UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 8-K

CURRENT REPORT

**PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934**

Date of Report (Date of earliest event reported): January 19, 2007

ALCOA INC.

(Exact name of Registrant as specified in its charter)

Pennsylvania	**1-3610**	**25-0317820**
(State or Other Jurisdiction of Incorporation)	**(Commission File Number)**	**(I.R.S. Employer Identification Number)**

390 Park Avenue, New York, New York	**10022-4608**
(Address of Principal Executive Offices)	**(Zip Code)**

Office of Investor Relations 212-836-2674
Office of the Secretary 412-553-4707
(Registrant's telephone number, including area code)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

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

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

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

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

Item 8.01. Other Events.

The financial information included as exhibits to this Current Report on Form 8-K updates certain portions of the Annual Report on Form 10-K for Alcoa Inc. (“Alcoa”) for the year ended December 31, 2005 and Forms 10-Q for the quarters ended March 31, 2006 and June 30, 2006 (collectively, the “Reports”) to reclassify the results of certain discontinued operations.

Certain financial information in the Annual Report on Form 10-K for the year ended December 31, 2005 has been updated to reflect the home exteriors business and the Hawesville, KY automotive casting facility in discontinued operations. In addition, Schedule II, “Valuation and Qualifying Accounts,” and Exhibit 12, “Computation of Ratio of Earnings to Fixed Charges,” to Alcoa’s Form 10-K for the year ended December 31, 2005 have been updated to reflect the home exteriors business and the Hawesville, KY automotive casting facility in discontinued operations.

Certain financial information in Forms 10-Q for the quarters ended March 31, 2006 and June 30, 2006 has been updated to reflect the home exteriors business in discontinued operations. The Hawesville, KY automotive casting facility was already reflected in discontinued operations at the time of the original filing of the Forms 10-Q for the quarters ended March 31, 2006 and June 30, 2006.

No attempt has been made to update other matters in the Reports. The reclassifications have no effect on Alcoa’s reported net income in the Reports.

During the third quarter of 2006, Alcoa entered into an agreement to sell its home exteriors business to Ply Gem Industries, Inc. for more than $300 million in cash. In accordance with Statement of Financial Accounting Standards No. 144, “*Accounting for the Impairment or Disposal of Long Lived Assets*,” (SFAS 144) Alcoa reported the operations of its home exteriors business as discontinued operations for each period presented in its Quarterly Report on Form 10-Q for the period ended September 30, 2006. In addition, the assets and related liabilities of the home exteriors business were classified as held for sale for each period presented in its Quarterly Report on Form 10-Q for the period ended September 30, 2006. The sale of the home exteriors business was completed in October 2006.

During the first quarter of 2006, Alcoa closed its Hawesville, KY automotive casting facility. In accordance with SFAS 144, Alcoa reported the operations of the Hawesville, KY automotive casting facility as discontinued operations and its assets and related liabilities were classified as held for sale for each period presented in its Quarterly Report on Form 10-Q for the period ended March 30, 2006.

The attached information should be read together with Alcoa’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2006.

The Reports, Schedule II and Exhibit 12 are attached as Exhibits 99.1 thru 99.5, and are incorporated herein by reference.

* * * * *

Forward-Looking Statements

Certain statements in the exhibits attached hereto relate to future events and expectations and as such constitute forward-looking statements. Forward-looking statements also include those containing such words as “anticipates,” “believes,” “estimates,” “expects,” “hopes,” “targets,” “should,” “will,” “will likely result,” “forecast,” “outlook,” “projects” or similar expressions. Such forward-looking statements

involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of Alcoa to be different from those expressed or implied in the forward-looking statements. Alcoa disclaims any intention or obligation, other than as required by law, to update or revise any forward-looking statements. Important factors that could cause actual results to differ materially from those in the forward-looking statements include: (a) material adverse changes in economic or aluminum industry conditions generally, including global supply and demand conditions and prices for primary aluminum, alumina and other products; (b) material adverse changes in the markets served by Alcoa, including the transportation, building, construction, distribution, packaging, industrial gas turbine and other markets; (c) Alcoa's inability to mitigate impacts from increased energy and raw materials costs, or other cost inflation; (d) Alcoa's inability to achieve the level of cost savings, productivity improvements or earnings or revenue growth anticipated by management; (e) Alcoa's inability to complete its growth projects and integration of acquired facilities as planned and by targeted completion dates; (f) unfavorable changes in laws, governmental regulations or policies, currency exchange rates or competitive factors in the countries in which Alcoa operates; (g) significant legal proceedings or investigations adverse to Alcoa, including environmental, product liability, safety and health and other claims; and (h) the other risk factors summarized in Alcoa's Form 10-K for the year ended December 31, 2005, Forms 10-Q for the quarters ended March 31, 2006, June 30, 2006 and September 30, 2006, and other reports filed with the Securities and Exchange Commission.

Item 9.01. Financial Statements and Exhibits.

(d) Exhibits.

The following are filed as exhibits to this report:

15	Letter Regarding Unaudited Interim Financial Information.
23	Consent of Independent Registered Public Accounting Firm.
99.1	Updated financial information in the Annual Report on Form 10-K for the year ended December 31, 2005.
99.2	Updated financial information in Schedule II of Form 10-K for the year ended December 31, 2005.
99.3	Updated financial information in Exhibit 12 of Form 10-K for the year ended December 31, 2005.
99.4	Updated financial information in the Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.
99.5	Updated financial information in the Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
99.6	Report of Independent Registered Public Accounting Firm on Financial Statement Schedule.

SIGNATURES

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

ALCOA INC.

By: /s/ Charles D. McLane, Jr.
Charles D. McLane, Jr.
Vice President and Chief Financial Officer

Dated: January 19, 2007

EXHIBIT INDEX

Exhibit No.	Description
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99.3	Updated financial information in Exhibit 12 of Form 10-K for the year ended December 31, 2005.
99.4	Updated financial information in the Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.
99.5	Updated financial information in the Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
99.6	Report of Independent Registered Public Accounting Firm on Financial Statement Schedule.

EXHIBIT 15

January 15, 2007

Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

RE: Alcoa Inc.

Commissioners:

We are aware that our report dated April 26, 2006, except with respect to the effects of the discontinued operations discussed in Note H, as to which the date is January 15, 2007, and our report dated July 26, 2006, except with respect to the effects of the discontinued operations discussed in Note H, as to which the date is January 15, 2007 on our reviews of interim financial information of Alcoa Inc. and its subsidiaries (Alcoa) for the three-month periods ended March 31, 2006 and 2005, and for the three and six-month periods ended June 30, 2006 and 2005, respectively, included in this Current Report on Form 8-K, are incorporated by reference in Alcoa's Registration Statements on Form S-8 (Nos. 33-24846, 333-32516, 333-106411, 33-22346, 33-49109, 33-60305, 333-27903, 333-62663, 333-79575, 333-36208, 333-37740, 333-39708, 333-115717, and 333-128445) and Form S-3 (No. 333-74874).

Very truly yours,

/s/PricewaterhouseCoopers LLP
Pittsburgh, Pennsylvania

EXHIBIT 23

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statements on Form S-3 (No. 333-74874) and Form S-8 (Nos. 33-22346, 33-24846, 33-49109, 33-60305, 333-27903, 333-62663, 333-79575, 333-32516, 333-36208, 333-37740, 333-39708, 333-106411, 333-115717 and 333-128445) of Alcoa Inc. and its subsidiaries of our reports dated February 17, 2006, except with respect to our opinion on the consolidated financial statements insofar as it relates to the effects of the discontinued operations discussed in Note B, as to which the date is January 15, 2007, relating to the financial statements, financial statement schedule, management's assessment of the effectiveness of internal control over financial reporting and the effectiveness of internal control over financial reporting, which appears in this Form 8-K.

/s/ PricewaterhouseCoopers LLP

Pittsburgh, Pennsylvania
January 15, 2007

Selected Financial Data

(in millions, except per-share amounts and ingot prices)

For the year ended December 31	2005	2004	2003	2002	2001
Sales	$25,568	$22,609	$20,282	$19,164	$21,190
Income from continuing operations	1,257	1,369	1,012	478	911
Loss from discontinued operations	(22)	(59)	(27)	(92)	(3)
Cumulative effect of accounting changes	(2)	—	(47)	34	—
Net income	1,233	1,310	938	420	908
Earnings (loss) per share:					
Basic:					
Income from continuing operations	1.44	1.57	1.18	.56	1.06
Loss from discontinued operations	(.03)	(.07)	(.03)	(.11)	—
Cumulative effect of accounting changes	—	—	(.06)	.04	—
Net income	1.41	1.50	1.09	.49	1.06
Diluted:					
Income from continuing operations	1.43	1.56	1.18	.56	1.05
Loss from discontinued operations	(.03)	(.07)	(.04)	(.11)	—
Cumulative effect of accounting changes	—	—	(.06)	.04	—
Net income	1.40	1.49	1.08	.49	1.05
Alcoa’s average realized price per metric ton of aluminum ingot	2,044	1,867	1,543	1,455	1,587
LME average 3-month price per metric ton of aluminum ingot	1,900	1,721	1,428	1,365	1,454
Cash dividends paid per common share	.60	.60	.60	.60	.60
Total assets	33,696	32,609	31,711	29,810	28,355
Short-term borrowings	300	267	50	34	163
Commercial paper	912	630	—	665	220
Long-term debt	5,337	5,402	7,216	7,784	6,264

The financial information for all prior periods has been reclassified to reflect assets held for sale and discontinued operations. See Note B to the Consolidated Financial Statements for further information.

In addition to the operational results presented in Management’s Discussion and Analysis of Financial Condition and Results of Operations, other significant items that impacted results included, but were not limited to, the following:

2005: Acquisitions and dispositions of businesses, restructuring and other charges, the sale of investments, and a tax benefit resulting from the finalization of certain tax reviews and audits
2004: Disposition of businesses, restructuring and other charges, changes in the provision for income taxes, the restructuring of debt and associated settlement of interest rate swaps, the effects of the Bécancour strike, the sale of a portion of Alcoa’s interest in the Juruti bauxite project, environmental charges, the termination of an alumina tolling arrangement, and discontinued operations
2003: Acquisitions and dispositions of businesses, restructuring and other charges, insurance settlements related to environmental matters, changes in the provision for income taxes, discontinued operations, and the adoption of a new accounting standard
2002: Restructuring and other charges, the adoption of new accounting standards, goodwill impairment, and discontinued operations
2001: Restructuring and other charges, dispositions of businesses, and various charges to cost of goods sold and selling, general administrative, and other expenses

The data presented in the Selected Financial Data table should be read in conjunction with the information provided in Management’s Discussion and Analysis of Financial Condition and Results of Operations and the Notes to the Consolidated Financial Statements.

Management's Discussion and Analysis of Financial Condition and Results of Operations

(dollars in millions, except per-share amounts and ingot prices; shipments in thousands of metric tons [mt])

Overview

Our Business

Alcoa is the world's leading producer of primary aluminum, fabricated aluminum, and alumina, and is active in all major aspects of the industry: technology, mining, refining, smelting, fabricating, and recycling. Aluminum is a commodity that is traded on the London Metal Exchange (LME) and priced daily based on market supply and demand. Aluminum and alumina represent approximately three-fourths of Alcoa's revenues, and the price of aluminum influences the operating results of Alcoa. Nonaluminum products include precision castings, industrial fasteners, consumer products, food service and flexible packaging products, plastic closures, and electrical distribution systems for cars and trucks. Alcoa's products are used worldwide in aircraft, automobiles, commercial transportation, packaging, consumer products, building and construction, and industrial applications.

Alcoa is a global company operating in 42 countries. North America is the largest market with 61% of Alcoa's revenues. Europe is also a significant market with 24% of the company's revenues. In addition, Alcoa has investments and activities in Australia, Brazil, China, Iceland, Jamaica, Russia, and Trinidad, which present opportunities for substantial growth. Governmental policies and other economic factors, including inflation and fluctuations in foreign currency exchange rates and interest rates, affect the results of operations in these countries.

Management Review of 2005 and Outlook for the Future

Alcoa aspires to be the best company in the world. As part of that mission, Alcoa strives to attain certain financial goals to improve both short-term and long-term profitability, while positioning the company to be successful in the future.

In 2005, Alcoa focused on long-term value creation through living our values, executing our growth strategy, controlling costs and capital, and strategically managing our portfolio of businesses. These actions contributed to the following achievements:

- Highest annual sales in company history of $25,568, reflecting revenue growth of $2,959, or 13%, over 2004;
- Income from continuing operations of $1,257, despite the challenge of significantly higher expenses for raw materials, energy, and other cost inflation;
- Cash from operations of $1,676, including a $300 discretionary pension contribution;
- Continued execution of our growth strategy, with significant investments in refinery expansions, smelter expansions and modernizations, as well as new smelter construction in Iceland; and
- Debt-to-capital ratio of 30.8%, well within our target range of 25% to 35%, considering $2,138 in capital expenditures.

In 2005, the company's results were positively impacted by the following: higher realized prices for aluminum and alumina; higher demand in downstream markets, particularly in higher value-added markets such as aerospace and commercial transportation; the sale of Alcoa's stake in Elkem ASA; an income tax benefit resulting from the finalization of certain tax reviews and audits; and the sale of railroad assets. In 2005, Alcoa's revenues rose to the highest level in company history while the company continued to significantly expand and plan future growth. During 2005, the company was also faced with a number of challenges, including higher than expected costs for energy and raw materials, restructuring costs driven by a new global business structure designed to optimize operations, integration of the acquired Russian facilities, the impact of Gulf Coast hurricanes, and business interruptions due to unplanned outages and labor strikes in Europe.

As we look to 2006 and beyond, we will work toward the following goals:

- Managing our portfolio of businesses by monitoring the progress of underperforming assets and making appropriate adjustments to strengthen the portfolio;
- Capitalizing on strong markets, using technology as an advantage, and continuing to fully integrate investments in Russia and China;
- Expanding our global reach to better serve customers, to improve competitiveness, and to grow our businesses. Alcoa is taking the following actions to achieve these goals: purchasing fabricating facilities in Russia and a rolling mill in China; expanding rolling capacity in the U.S. and England; and positioning our primary businesses lower on the cost curve by (i) opening a bauxite mine in Brazil, (ii) expanding alumina refinery capacity in Australia, Jamaica, and Brazil, (iii) expanding smelting capacity in Brazil, and (iv) constructing a smelter in Iceland and an anode facility in Norway. Capital expenditures for these major growth projects and other sustaining projects are projected to be in the range of $2,500 to $3,000 in 2006. These projects are outlined in more detail under Segment Information, Liquidity and Capital Resources, and Contractual Obligations and Off-Balance Sheet Arrangements; and
- Continuing to drive operational excellence through deployment of the Alcoa Business System (ABS), while focusing on cost savings to offset increased energy and input costs for raw materials.

Forward-Looking Statements

Certain statements in this report under this caption and elsewhere relate to future events and expectations and, as such, constitute forward-looking statements. Forward-looking statements also include those containing such words as "anticipates," "believes," "estimates," "expects," "hopes," "targets," "should," "will," "will likely result," "forecast," "outlook," "projects," or similar expressions. Such forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause actual results, performance, or achievements of Alcoa to be different from those expressed or implied in the forward-looking statements. For a discussion of some of the specific factors that may cause such a difference, see Notes N and Y to the Consolidated Financial Statements and the disclosures included under

Segment Information and Market Risks and Derivative Activities. For additional information on forward-looking statements and risk factors, see Alcoa's Form 10-K, Part I, Item 1A. Alcoa disclaims any intention or obligation (other than as required by law) to update or revise any forward-looking statements.

Results of Operations

Earnings Summary

Alcoa's income from continuing operations for 2005 was $1,257, or $1.43 per diluted share, compared with $1,369, or $1.56 per share in 2004. The highlights for 2005 include: higher realized prices for alumina and aluminum as LME prices increased by 10% over 2004 levels; increased sales across all segments; higher demand in upstream businesses and in downstream businesses serving the aerospace, commercial transportation, industrial products, distribution, packaging, and building and construction markets; a $180 net gain related to the sale of Alcoa's stake in Elkem ASA; a $120 tax benefit related to the finalization of certain tax reviews and audits during the second quarter of 2005; and a $37 gain on the sale of railroad assets.

These positive contributions were more than offset in 2005 by the following: significant cost increases for energy and raw materials; the impact of a weakened U.S. dollar against other currencies, primarily the Canadian dollar and the Euro; restructuring charges of $190 associated with the global realignment of Alcoa's organization structure designed to streamline operations; operating losses of $69 related to the acquired facilities in Russia; a $58 charge for the closure of the Hamburger Aluminium-Werk facility in Germany; an increase in environmental reserves, principally related to the closed East St. Louis, IL facility; an increase in legal reserves, primarily due to litigation involving a closed Howmet facility; and higher costs associated with hurricanes and business interruptions.

Net income for 2005 was $1,233, or $1.40 per diluted share, compared with $1,310, or $1.49 per share, in 2004. Net income of $1,233 in 2005 included losses from discontinued operations of $22, comprised of $21 in net operating income, offset by $43 related to net losses on businesses impaired or sold.

Alcoa's income from continuing operations for 2004 was $1,369, or $1.56 per diluted share, compared with $1,012, or $1.18 per share, in 2003. The increase in income from continuing operations was primarily due to higher realized prices for alumina and aluminum; improved profitability across five of six segments; a $38 gain related to the retirement of debt and associated interest rate swap settlement; a $37 gain on the sale of a portion of Alcoa's interest in the Juruti bauxite project to Alumina Limited; continued focus on completion of divestitures, which included a $61 gain on the sale of the specialty chemicals business; and a $15 gain from the termination of an alumina tolling arrangement. Partially offsetting these increases were higher energy and raw materials costs, the unfavorable impact of the U.S. dollar against foreign currencies, the impact of a strike at the Bécancour smelter; a $41 increase in environmental and legal reserves, principally related to the Grasse River site and El Campo, and the absence of $79 in insurance settlements that occurred in 2003.

Net income for 2004 was $1,310, or $1.49 per diluted share, compared with $938, or $1.08 per share, in 2003. Net income of $1,310 in 2004 included losses of $59 in discontinued operations, comprised of $89 in impairment charges to reflect the estimated fair values of the protective packaging business, the telecommunications business, and a small casting business, somewhat offset by net operating income of $25 and a net gain of $5 on divested businesses.

Sales—Sales for 2005 were $25,568 compared with sales of $22,609 in 2004, an increase of $2,959, or 13%. The 9% increase in the realized price of aluminum and the 14% increase in the realized price of alumina contributed to the increase in sales over the prior year, as approximately one-half of the increase in sales was due to higher realized prices. Demand increased in upstream businesses and in downstream businesses serving the aerospace, commercial transportation, industrial products, distribution, packaging, and building and construction markets. The acquisition of two Russian fabricating facilities provided $449 in additional revenue in 2005. In addition, higher sales related to metal purchased and subsequently resold and favorable foreign currency exchange movements positively impacted 2005. These positive contributions more than offset the sales decreases from the divestitures in 2004 of Alcoa's specialty chemicals business, the Russellville, AR and St. Louis, MO foil facilities, and the European and Brazilian extrusion facilities.

Sales in 2004 were $22,609 compared with sales of $20,282 in 2003, an increase of $2,327, or 11%. The 21% increase in the realized price of aluminum and 23% increase in the realized price of alumina contributed significantly to the increase in sales over the prior year, as two-thirds of the increase in sales was due to higher realized prices. Demand increased in downstream businesses serving the commercial transportation, building and construction, aerospace, and packaging markets. In addition, the acquisition of the remaining 50% of KAAL Australia in October 2003 provided $370 in additional revenue in 2004. Partly offsetting these increases were sales decreases due to the divestitures noted above.

Cost of Goods Sold—COGS as a percentage of sales was 81.0% in 2005 compared with 79.3% in 2004. Increased realized prices for alumina and aluminum and higher volumes were more than offset by increased costs for raw materials and energy, Russian operating costs, unfavorable foreign currency exchange movements, costs associated with hurricanes and business interruptions, and an increase in environmental and legal reserves.

COGS as a percentage of sales was 79.3% in 2004 compared with 79.4% in 2003. Increased realized prices for alumina and aluminum, higher volumes, and cost savings were mostly offset by higher costs associated with energy and raw materials, the

Bécancour strike, an increase of $42 in environmental reserves, and unfavorable foreign currency exchange movements.

Selling, General Administrative, and Other Expenses—SG&A expenses were $1,295, or 5.1% of sales, in 2005 compared with $1,194, or 5.3% of sales, in 2004. Expenses increased by $101 primarily due to the acquisition of two Russian facilities.

SG&A expenses were $1,194, or 5.3% of sales, in 2004 compared with $1,173, or 5.8% of sales, in 2003. Expenses increased by $21 due to unfavorable foreign currency exchange movements, increased bad debt expense, and stock awards granted in 2004, somewhat offset by lower deferred compensation costs.

Research and Development Expenses—R&D expenses were $192 in 2005 compared with $178 in 2004 and $187 in 2003. The increase in 2005 was principally due to increased spending in the Primary Metals segment related to inert anode technology. The decrease in 2004 compared with 2003 was primarily driven by Alcoa's continued focus to reduce spending and control costs.

Provision for Depreciation, Depletion, and Amortization—The provision for depreciation, depletion, and amortization was $1,256 in 2005 compared with $1,177 in 2004. The increase of $79, or 7%, was primarily caused by a higher asset base due to the acquisition of two Russian fabricating facilities and unfavorable foreign currency exchange movements.

The provision for depreciation, depletion, and amortization was $1,177 in 2004 compared with $1,149 in 2003. The increase of $28, or 2%, was primarily caused by unfavorable foreign currency exchange movements.

Restructuring and Other Charges—Restructuring and other charges for each of the three years in the period ended December 31, 2005, were comprised of:

	2005	2004	2003
Asset impairments	$ 86	$ 6	$ —
Layoff costs	238	40	44
Other costs	16	—	—
Gain on sale of specialty chemicals business	—	(53)	—
Net reversals of previously recorded layoff and other costs*	(48)	(15)	(38)
Net reversals of previously recorded gains/losses on assets held for sale	—	—	(33)
Restructuring and other charges	$292	$(22)	$(27)

*Reversals of previously recorded layoff and other costs resulted from changes in facts and circumstances that led to changes in estimated costs.

2005 Restructuring Program—As a result of the global realignment of Alcoa's organization structure, designed to optimize operations in order to better serve customers, a restructuring plan was developed to identify opportunities to streamline operations on a global basis. The restructuring program consisted of the elimination of jobs across all segments of the company, various plant closings and consolidations, and asset disposals. Restructuring charges of $292 ($190 after tax and minority interests) were recorded in 2005 and were comprised of the following components: $238 of charges for employee termination and severance costs associated with approximately 8,450 salaried and hourly employees, spread globally across the company; $86 related to asset impairments for structures, machinery, and equipment; and $16 for exit costs, consisting primarily of accelerated depreciation associated with assets for which the useful life has been changed due to plans to close certain facilities in the near term. Reversals of previously recorded layoff and other costs were primarily due to Alcoa's decision to sell certain locations that it previously planned to shut down in 2005. Alcoa expects the implementation of this restructuring plan to eliminate approximately $200 (pretax) from its cost base when completed.

Alcoa does not include restructuring and other charges in the segment results. The pretax impact of allocating restructuring and other charges to the segment results would have been:

	2005	2004	2003
Alumina	$ 6	$(48)	$ (1)
Primary Metals	36	(1)	4
Flat-Rolled Products	15	1	13
Extruded and End Products	70	9	7
Engineered Solutions	109	8	(11)
Packaging and Consumer	39	10	(44)
Segment total	275	(21)	(32)
Corporate	17	(1)	5
Total restructuring and other charges	$292	$(22)	$(27)

The following discussion details the significant components of the 2005 restructuring program:

– In December 2005, the company temporarily curtailed production at its Eastalco, MD smelter because it was not able to secure a new, competitive power supply for the facility. A

charge of $14 was recorded for the termination of approximately 550 people.

– The automotive operations, included in the Engineered Solutions segment, were restructured to improve efficiencies and included the following actions:

- A restructuring of the cast auto wheels business occurred, which ultimately included the sale of the wheels facility in Italy. Total charges recorded in 2005 were $71, consisting of $15 for severance costs associated with approximately 450 employees, $46 for asset impairments, and $10 loss on sale of the facility in Italy.
- Headcount reductions in the AFL automotive business resulted in a charge of $27 for the termination of approximately 3,900 employees, primarily in Mexico.

– The global extruded and end products businesses were restructured to optimize operations and increase productivity and included the following actions:

- Headcount reductions across various businesses resulted in a charge of $50 for the termination of 1,050 employees in the U.S., Europe, and Latin America.
- Charges of $15 were recorded for asset disposals at various U.S. and European extrusion plants related to certain assets which the businesses have ceased to operate.

– The restructuring associated with the packaging and consumer businesses consisted of plant consolidations and closures designed to strengthen the operations, resulting in charges of $39, comprised of $23 for the termination of 1,620 employees primarily in the U.S., $8 for asset disposals, and $8 for other exit costs. Other exit costs primarily consisted of accelerated depreciation.

Employee termination and severance costs were recorded based on approved detailed action plans submitted by the operating locations that specified positions to be eliminated, benefits to be paid under existing severance plans, union contracts or statutory requirements, and the expected timetable for completion of the plans. These terminations are expected to be completed in the next twelve months. As of December 31, 2005, 3,550 of the approximately 8,450 employees had been terminated. Approximately $69 of cash payments were made against the 2005 program reserves in 2005.

2004 Restructuring Program—During 2004, Alcoa recorded income of $22 ($41 after tax and minority interests) for restructuring and other items. The income recognized was comprised of the following components: a gain of $53 ($61 after tax and minority interests) on the sale of Alcoa's specialty chemicals business and $15 resulting from adjustments to prior year reserves; offset by charges of $40 related to additional layoff reserves associated with approximately 4,100 hourly and salaried employees (located primarily in Mexico and the U.S.), as the company continued to focus on reducing costs; and $6 of asset impairments. The 2004 restructuring program is essentially complete. Approximately $16 of cash payments were made in 2005 related to prior year restructuring programs.

2003 Restructuring Program—During 2003, Alcoa recorded income of $27 ($25 after tax and minority interests) for restructuring and other charges. The income recognized was comprised of the following components: $44 of charges for employee termination and severance costs associated with approximately 1,600 hourly and salaried employees (located primarily in Europe, the U.S., and Brazil), as the company continued to focus on cost reductions in businesses that continued to be impacted by market declines; $33 of net favorable adjustments on assets held for sale; and $38 of income resulting from adjustments to prior year layoff reserves due to changes in facts and circumstances that led to changes in estimated costs. The 2003 restructuring program is essentially complete.

Interest Expense—Interest expense was $339 in 2005 compared with $271 in 2004, resulting in an increase of $68, or 25%. This increase was principally caused by higher average effective interest rates and increased borrowings, somewhat offset by an increase in interest capitalized.

Interest expense was $271 in 2004 compared with $314 in 2003, resulting in a decrease of $43, or 14%. This decrease was principally caused by lower average debt levels.

Other Income—Other income was $480 in 2005 compared with $270 in 2004. The increase of $210, or 78%, was primarily due to the gain of $345 on the sale of Alcoa's stake in Elkem ASA and the $67 gain on the sale of railroad assets, partially offset by the $90 charge for impairment, layoff, and other costs related to the closure of the Hamburger Aluminium-Werk facility in Germany and the absence of the $58 gain on the early retirement of debt that occurred in 2004.

Other income of $270 in 2004 was relatively flat compared with $273 in 2003. In 2004, a $58 gain recognized on the early retirement of debt, a $53 change in favorable foreign currency exchange movements, and a $35 gain on the termination of an alumina tolling arrangement were mostly offset by the $105 gain in 2003 from insurance settlements of a series of historical environmental matters in the U.S., as well as a decrease in the cash surrender value of employee life insurance, among other smaller items.

Income Taxes—Alcoa's effective tax rate was 23% in 2005 compared with the statutory rate of 35% and Alcoa's effective tax rates of 25% in 2004 and 24% in 2003. The effective tax rate in 2005 reflects two significant discrete tax items:

- A $43 tax impact of recognizing the previously undistributed equity earnings related to Alcoa's stake in Elkem ASA increased the rate by approximately 2.2 percentage points.
- The finalization of certain tax reviews and audits decreased the rate by approximately 6.2 percentage points.

Management anticipates that the tax rate in 2006 will be similar to the tax rates for 2005 and 2004 excluding the impact of discrete tax items.

In October of 2004, the American Job Creation Act of 2004 (AJCA) was signed into law. Alcoa did not utilize the AJCA provision that allows companies to repatriate earnings from foreign subsidiaries at a reduced U.S. tax rate.

Minority Interests—Minority interests' share of income from operations was $259 in 2005 compared with $245 in 2004. The $14 increase was primarily due to higher earnings at Alcoa World Alumina and Chemicals (AWAC), attributed primarily to higher realized prices.

Minority interests' share of income from operations was $245 in 2004 compared with $238 in 2003. The $7 increase in 2004 was due to higher earnings at AWAC, attributed to higher realized prices, increased volumes, and the gain associated with the termination of an alumina tolling arrangement. This increase was partially offset by Alcoa's acquisition of the minority interest in Alcoa Alumínio in August 2003 and the sale of the specialty chemicals business in 2004.

Loss From Discontinued Operations—Loss from discontinued operations was $22 in 2005 compared with losses of $59 in 2004 and $27 in 2003. The loss of $22 in 2005 was comprised of $21 in net operating income, offset by $43 of net losses associated with businesses impaired or sold in 2005, including a $28 loss for asset impairments associated with the Hawesville, KY automotive casting facility. The loss of $59 in 2004 was comprised of $89 in impairment charges to reflect the estimated fair values of the protective packaging business, the telecommunications business, and a small casting business, somewhat offset by $25 in net operating income and a net gain of $5 on divested businesses. The loss of $27 in 2003 was comprised of an impairment of $45 related to a reduction in the estimated fair value of the automotive fasteners business, somewhat offset by $18 of operating income. See Note B to the Consolidated Financial Statements for further information.

In the third quarter of 2006, Alcoa reclassified its home exteriors business to discontinued operations upon the signing of a definitive sale agreement with Ply Gem Industries, Inc. In the first quarter of 2006, Alcoa reclassified the Hawesville, KY automotive casting facility to discontinued operations upon closure of the facility. The results of the Extruded and End Products segment and the Engineered Solutions segment have been reclassified to reflect the movement of the home exteriors business and the automotive casting facility, respectively, into discontinued operations.

In the third quarter of 2005, Alcoa reclassified the imaging and graphic communications business of Southern Graphic Systems, Inc. (SGS) to discontinued operations based on the decision to sell the business. The results of the Packaging and Consumer segment have been reclassified to reflect the movement of this business into discontinued operations. In December 2005, Alcoa completed the sale of SGS to Citigroup Venture Capital Equity Partners, LP for $408 in cash and recognized an after-tax gain of $9.

In 2004, Alcoa also identified businesses to be divested so as to better focus on its core capabilities. The divestitures of the telecommunications business and the protective packaging business were completed in 2005. See Note F to the Consolidated Financial Statements for additional information.

Cumulative Effect of Accounting Changes—Effective December 31, 2005, Alcoa adopted Financial Accounting Standards Board (FASB) Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" (FIN 47) and recorded a cumulative effect adjustment of $2, consisting primarily of costs for regulated waste materials related to the demolition of certain power facilities.

In 2003, Alcoa adopted Statement of Financial Accounting Standards (SFAS) No. 143, "Accounting for Asset Retirement Obligations" and recorded a cumulative effect adjustment of $47, consisting primarily of costs to establish assets and liabilities related to spent pot lining disposal for pots currently in operation. See Note C to the Consolidated Financial Statements for further information.

Segment Information

Alcoa's operations consist of six worldwide segments: Alumina, Primary Metals, Flat-Rolled Products, Extruded and End Products, Engineered Solutions, and Packaging and Consumer. Alcoa's management reporting system measures the after-tax operating income (ATOI) of each segment. Certain items, such as interest income, interest expense, foreign currency translation gains/losses, certain effects of LIFO inventory accounting, minority interests, restructuring and other charges, discontinued operations, and accounting changes are excluded from segment ATOI. In addition, certain expenses, such as corporate general administrative expenses and depreciation and amortization on corporate assets, are not included in segment ATOI. Segment assets exclude cash, cash equivalents, short-term investments, and all deferred taxes. Segment assets also exclude items such as corporate fixed assets, LIFO reserves, goodwill allocated to corporate, assets held for sale, and other amounts.

ATOI for all segments totaled $2,139 in 2005, $2,105 in 2004, and $1,704 in 2003. See Note Q to the Consolidated Financial Statements for additional information. The following discussion provides shipments, sales, and ATOI data of each segment for each of the three years in the period ended December 31, 2005. The financial information and data on shipments for all prior periods have been reclassified for discontinued operations.

In January 2005, Alcoa realigned its organization structure, creating global groups to better serve customers and increase the ability to capture efficiencies. As a result, certain reportable segments have been reorganized to reflect the new organization. The businesses within the former Engineered Products segment and the Other "group" have been realigned to form the new Extruded and End Products segment and the new Engineered Solutions segment. Prior period amounts have been reclassified to reflect these changes. Additionally, the Alumina and Chemicals segment has been renamed the Alumina segment, to reflect the sale of the specialty chemicals business.

Alumina

	2005	2004	2003
Alumina production (mt)	14,598	14,343	13,841
Third-party alumina shipments (mt)*	7,857	8,062	8,101
Third-party sales	$2,130	$1,975	$2,002
Intersegment sales	1,707	1,418	1,021
Total sales	$3,837	$3,393	$3,023
ATOI	$ 682	$ 632	$ 415

* Alumina shipments have been restated to reflect total alumina shipments rather than only smelter-grade alumina shipments.

This segment consists of Alcoa's worldwide alumina system that includes the mining of bauxite, which is then refined into alumina. Alumina is sold directly to internal and external smelter customers worldwide or is processed into industrial chemical products. Alcoa's alumina operations in Australia are a significant component of this segment. Slightly more than half of Alcoa's alumina production is sold under supply contracts to third parties worldwide, while the remainder is used internally. Alcoa's specialty chemicals business was sold in the first quarter of 2004.

In 2005, alumina production increased by 255,000 mt, resulting primarily from increased production in the Poços de Caldas refinery in Brazil (13% increase in production) and the Kwinana, Australia refinery (10% increase in production) and the capacity expansion in Jamaica (5% increase in production). In 2004, alumina production increased by 502,000 mt, resulting primarily from the capacity expansion in Jamaica (14% increase in production) and the restart of capacity at Point Comfort, TX (13% increase in production), as well as an 11% increase in production at the San Ciprián, Spain refinery.

Third-party sales for the Alumina segment increased $155, or 8%, in 2005 compared with 2004, primarily due to a 14% increase in realized price influenced by higher LME prices, which was somewhat offset by lower third-party volumes. Third-party sales remained relatively flat in 2004 compared with 2003. The increase in realized prices of 23% in 2004 was more than offset by lower third-party volumes due to the expiration of an alumina purchase agreement in 2003, which resulted in higher intersegment sales in 2004. Also, the sale of the specialty chemicals business in 2004 negatively impacted sales by $287.

ATOI for this segment rose 8% in 2005 compared with 2004, primarily due to higher realized prices and increased total volumes. These positive contributions were somewhat offset by higher raw materials, energy, and maintenance costs; unfavorable foreign currency exchange movements; the absence of a $37 gain on the sale of a portion of Alcoa's interest in a Brazil bauxite project that occurred in 2004; and the absence of a $15 gain on the termination of an alumina tolling arrangement that occurred in 2004. ATOI for this segment rose 52% in 2004 compared with 2003, primarily due to higher realized prices, increased total volumes, and gains totaling $52 as previously mentioned. These positive contributions were somewhat offset by unfavorable foreign currency exchange movements, higher raw material costs, and the loss of profit associated with the sale of the specialty chemicals business.

In 2006, Alcoa will continue its brownfield projects at refineries in Brazil (addition of 2,100,000 mt—1,134,000 mt is Alcoa's share); Pinjarra, Western Australia (657,000 mt addition); and Jamaica (addition of 1,500,000 mt). Higher raw material costs are anticipated in 2006, and energy costs will be dependent on the cost of natural gas and fuel oil.

Primary Metals

	2005	2004	2003
Aluminum production (mt)	3,554	3,376	3,508
Third-party aluminum shipments (mt)	2,154	1,882	1,952
Alcoa's average realized price per metric ton of aluminum ingot	$2,044	$1,867	$1,543
Third-party sales	$4,698	$3,806	$3,229
Intersegment sales	4,808	4,335	3,098
Total sales	$9,506	$8,141	$6,327
ATOI	$ 822	$ 808	$ 657

This segment consists of Alcoa's worldwide smelter system. Primary Metals receives alumina primarily from the Alumina segment and produces aluminum ingot to be used by Alcoa's fabricating businesses, as well as sold to external customers, aluminum traders, and commodity markets. Results from the sale of aluminum powder, scrap, and excess power are also included in this segment, as well as the results of aluminum derivative contracts. Aluminum ingot produced by Alcoa and used internally is transferred to other segments at prevailing market prices. The sale of ingot represents approximately 90% of this segment's third-party sales. In 2005, aluminum production increased by 178,000 mt, principally due to the restart of the Massena, NY and Bécancour, Canada smelters, as well as the partial restart of the Wenatchee, WA smelter. In 2004, aluminum production decreased by 132,000 mt, principally due to the strike at the Bécancour facility.

Third-party sales for the Primary Metals segment increased 23% in 2005 compared with 2004, primarily due to an increase in realized prices of 9% and increased third-party shipments. Third-party sales increased 18% in 2004 compared with 2003, primarily due to an increase in realized prices of 21%, which more than offset lower third-party shipments. An electrical outage at the Alumar smelter in Brazil also had a negative impact on third-party sales in 2003. Intersegment sales increased 11% in 2005 and 40% in 2004 compared with previous periods due to higher realized prices and higher internal demand.

ATOI for this segment increased 2% in 2005 compared with 2004 as higher realized prices and increased volumes were mostly offset by increased raw materials and energy costs, unfavorable foreign currency exchange movements, and outages and restart costs. ATOI for this segment increased 23% in 2004 compared with 2003 as higher realized prices and higher total shipments were somewhat offset by the impact of unfavorable

foreign currency exchange movements, higher costs for energy and purchased metal, and the effects of a strike at Bécancour in 2004.

Alcoa currently has 509,000 metric tons per year (mtpy) of idle capacity on a base capacity of 4,004,000 mtpy. Idle capacity includes the temporary curtailment of the Eastalco smelter in Maryland. The Iceland smelter, which will add 346,000 mtpy of capacity, is expected to be completed in 2007. The completion of the expansion at the Alumar smelter in Brazil will also add approximately 63,000 mtpy of capacity. In 2005, the company continued construction on a new anode plant in Norway and began modernization of two Spanish smelters and the Poços de Caldas smelter in Brazil. In 2006, the additional capacity from restarts and growth projects will more than offset the reduction of capacity due to the temporary curtailment of the Eastalco smelter.

Flat-Rolled Products

	2005	2004	2003
Third-party aluminum shipments (mt)	2,156	2,046	1,819
Third-party sales	$6,836	$5,962	$4,815
Intersegment sales	128	89	66
Total sales	$6,964	$6,051	$4,881
ATOI	$ 288	$ 246	$ 221

This segment's principal business is the production and sale of aluminum plate, sheet, and foil. This segment includes rigid container sheet (RCS), which is sold directly to customers in the packaging and consumer market and is used to produce aluminum beverage cans. Seasonal increases in RCS sales are generally experienced in the second and third quarters of the year. This segment also includes sheet and plate used in the transportation, building and construction, and distributor markets (mainly used in the production of machinery and equipment and consumer durables), of which approximately two-thirds is sold directly to customers, while the remainder is sold through distributors. Approximately two-thirds of the third-party sales in this segment are derived from sheet and plate, and foil used in industrial markets, while the remaining one-third of third-party sales consists of RCS. While the customer base for flat-rolled products is large, a significant amount of sales of RCS, sheet, and plate is to a relatively small number of customers.

Third-party sales for the Flat-Rolled Products segment increased 15% in 2005 compared with 2004. The increase was primarily due to higher prices, higher volumes resulting from the acquisition of two Russian facilities, favorable mix for sheet and plate in the aerospace market, and increased volumes for RCS, as well as favorable foreign currency exchange movements. Third-party sales for the Flat-Rolled Products segment increased 24% in 2004 compared with 2003. The increase was due to the acquisition of the remaining 50% interest in KAAL Australia (can sheet rolling mills) in October of 2003, higher prices, the favorable impact of foreign currency exchange movements in Europe, and increased volumes for sheet and plate. Increased volumes for these products resulted from improved performance in businesses serving the commercial transportation, aerospace, and distribution markets.

ATOI for this segment increased 17% in 2005 compared with 2004, principally due to higher volumes, favorable mix for sheet and plate, higher prices, and increased productivity. These positive contributions were somewhat offset by increased raw material, energy, and transportation costs, as well as operating losses of $52 at the acquired Russian facilities. ATOI for this segment increased 11% in 2004 compared with 2003, principally due to higher volumes, higher prices, improved productivity, and favorable mix for sheet and plate; favorable foreign currency exchange movements in Europe; and the contribution of KAAL Australia. These positive contributions were somewhat offset by a hot mill interruption at the Kitts Green facility in the U.K. and temporary throughput issues at the Tennessee can sheet facility. These issues were resolved in 2004.

In 2006, operating costs at the Russian facilities are expected to decrease, and price pressure is expected in common alloy sheet.

Extruded and End Products

	2005	2004	2003
Third-party aluminum shipments (mt)	853	843	802
Third-party sales	$3,729	$3,387	$3,003
Intersegment sales	64	54	34
Total sales	$3,793	$3,441	$3,037
ATOI	$ 39	$ 62	$ 33

This segment consists of extruded products, some of which are further fabricated into a variety of end products, and includes hard- and soft-alloy extrusions and architectural extrusions. These products primarily serve the building and construction, distribution, aerospace, automotive, and commercial transportation markets. These products are sold directly to customers and through distributors.

Third-party sales for the Extruded and End Products segment increased 10% in 2005 compared with 2004, principally due to higher prices. The increase in volumes from the Russian facilities and the strength of the businesses serving the commercial building and construction market were somewhat offset by lower volumes and prices in Europe. Third-party sales increased 13% in 2004 compared with 2003, principally due to increased volumes in the building and construction market, higher prices, and favorable foreign currency exchange movements.

ATOI for this segment decreased 37% in 2005 compared with 2004, as higher prices and increased volumes in the businesses serving the commercial building and construction market were more than offset by higher raw materials and energy costs and lower volumes in Europe. In addition, this segment was negatively impacted by operating losses of $7 associated with integration costs for Russian extruded products.

ATOI for this segment increased 88% in 2004 compared with 2003, principally resulting from increased volumes due to improved market conditions as noted previously, higher prices, and strong productivity gains.

Engineered Solutions

	2005	2004	2003
Third-party aluminum shipments (mt)	145	126	104
Third-party sales	$5,032	$4,563	$4,325
ATOI	$ 203	$ 216	$ 190

This segment includes titanium, aluminum, and super-alloy investment castings; forgings and fasteners; electrical distribution systems; aluminum wheels; and integrated aluminum structural systems used in the aerospace, automotive, commercial transportation, and power generation markets. These products are sold directly to customers and through distributors.

Third-party sales for the Engineered Solutions segment increased 10% in 2005 compared with 2004. The increase was due primarily to increased volumes in the businesses serving the commercial transportation, aerospace, and industrial gas turbine markets. These positive contributions were somewhat offset by pricing pressures. Third-party sales increased 6% in 2004 compared with 2003, primarily due to higher prices and favorable foreign currency exchange movements.

ATOI for this segment decreased 6% in 2005 compared with 2004, as increased volumes and favorable mix in the businesses serving the aerospace market positively impacted results. This positive contribution was more than offset by increased raw materials costs, operating losses of $3 related to the acquired Russian facilities, increased litigation expenses related to a closed Howmet facility, the resolution of a local tax audit, and the adverse impact of a fire and business interruption at Howmet's Dover, NJ facility. ATOI increased 14% in 2004 compared with 2003, primarily due to productivity improvements in the automotive parts business and cost savings, which were slightly offset by decreased volumes and higher raw materials costs.

In 2006, the aerospace market is expected to remain strong, and automotive volumes are projected to increase, including AFL automotive.

Packaging and Consumer

	2005	2004	2003
Third-party aluminum shipments (mt)	151	164	167
Third-party sales	$3,139	$2,923	$2,894
ATOI	$ 105	$ 141	$ 188

This segment includes consumer, foodservice, and flexible packaging products; food and beverage closures; and plastic sheet and film for the packaging industry. The principal products in this segment include aluminum foil; plastic wraps and bags; plastic beverage and food closures; flexible packaging products; thermoformed plastic containers; and extruded plastic sheet and film. Consumer products are marketed under brands including Reynolds Wrap®, Diamond®, Baco®, and Cut-Rite® wax paper. Seasonal increases generally occur in the second and fourth quarters of the year for such products as consumer foil and plastic wraps and bags, while seasonal slowdowns for closures generally occur in the fourth quarter of the year. Products are generally sold directly to customers, consisting of supermarkets, beverage companies, food processors, retail chains, and commercial foodservice distributors.

Third-party sales for the Packaging and Consumer segment increased 7% in 2005 compared with 2004, principally due to higher prices, as Alcoa was able to pass through a significant amount of the increased resin costs. Increased volumes in the closures and consumer products businesses also positively impacted 2005 and were somewhat offset by a decrease in volumes in the plastic sheet and film business. Third-party sales for the Packaging and Consumer segment remained relatively flat in 2004 compared with 2003, as increased volumes in the closures and plastic sheet and film businesses and higher prices were offset by the impact of the sale of Alcoa's Latin America PET business.

ATOI for this segment decreased 26% in 2005 compared with 2004, as the increases in prices and volumes noted previously, along with productivity gains, were more than offset by higher raw materials costs and unfavorable mix in the consumer products and flexible packaging businesses. ATOI for this segment in 2004 decreased 25% compared with 2003, primarily due to significantly higher resin and metal costs, unfavorable foreign currency exchange movements, and the divestitures of the Latin America PET business and Latasa, which were somewhat offset by increased volumes as noted above.

In 2006, higher input costs are anticipated for resin and metal.

Reconciliation of ATOI to Consolidated Net Income— The following table reconciles segment ATOI to consolidated net income.

	2005	2004	2003
ATOI	$2,139	$2,105	$1,704
Impact of intersegment profit adjustments	37	52	9
Unallocated amounts (net of tax):			
Interest income	42	26	24
Interest expense	(220)	(176)	(204)
Minority interests	(259)	(245)	(238)
Corporate expense	(312)	(283)	(287)
Restructuring and other charges	(197)	23	26
Discontinued operations	(22)	(59)	(27)
Accounting changes	(2)	—	(47)
Other	27	(133)	(22)
Consolidated net income	$1,233	$1,310	$ 938

Items required to reconcile segment ATOI to consolidated net income include:

- Corporate adjustments to eliminate any remaining profit or loss between segments;
- The after-tax impact of interest income and expense;
- Minority interests;
- Corporate expense, comprised of general administrative and selling expenses of operating the corporate headquarters and other global administrative facilities, along with depreciation on corporate-owned assets;
- Restructuring and other charges (excluding minority interests);
- Discontinued operations;
- Accounting changes for conditional asset retirement obligations in 2005 and asset retirement obligations in 2003; and
- Other, which consists of the impact of LIFO, differences between estimated tax rates used in the segments and the corporate effective tax rate, and other nonoperating items such as foreign currency translation gains/losses.

The significant changes in the reconciling items between ATOI and consolidated net income for 2005 compared with 2004 consisted of:

- An increase in interest expense, primarily due to higher average effective interest rates and increased borrowings, somewhat offset by an increase in interest capitalized;
- A $220 increase in restructuring and other charges due to the company's 2005 global restructuring plan;
- A change in discontinued operations due to significant impairment losses recognized in 2004 on the protective packaging and telecommunications businesses; and
- An increase in Other, primarily due to the $180 net gain on the sale of Alcoa's stake in Elkem ASA and a $120 tax benefit related to the finalization of certain tax reviews and audits during the second quarter of 2005, slightly offset by the $58 charge related to the closure of the Hamburger Aluminium-Werk facility in Germany and an increase in LIFO inventory adjustments due to the increase in raw materials and energy costs.

The significant changes in the reconciling items between ATOI and consolidated net income for 2004 compared with 2003 consisted of:

- A decrease in interest expense, primarily due to lower average debt levels;
- An increase in the loss from discontinued operations due to the reclassification of the protective packaging business, the telecommunications business, and a small casting business to discontinued operations, which resulted in an $89 impairment loss in 2004 to reflect the estimated fair values of these businesses; and
- An increase in Other, principally caused by an increase in LIFO inventory adjustments due to the increase in the price of aluminum, as well as $79 lower proceeds from insurance settlements compared with 2003. Partially offsetting the increase are $49 in favorable foreign currency exchange movements and a $38 gain recognized on the restructuring of debt in 2004. See Note K to the Consolidated Financial Statements for additional information on this transaction.

Market Risks and Derivative Activities

In addition to the risks inherent in its operations, Alcoa is exposed to financial, market, political, and economic risks. The following discussion provides information regarding Alcoa's exposure to the risks of changing commodity prices, foreign exchange rates, and interest rates.

Alcoa's commodity and derivative activities are subject to the management, direction, and control of the Strategic Risk Management Committee (SRMC). The SRMC is composed of the chief executive officer, the chief financial officer, and other officers and employees that the chief executive officer selects. The SRMC reports to the Board of Directors on the scope of its activities.

All of the interest rate, foreign currency, aluminum and other commodity contracts are held for purposes other than trading. They are used primarily to mitigate uncertainty and volatility, and to cover underlying exposures. The company is not involved in energy-trading activities, weather derivatives, or other nonexchange commodity trading activities.

Commodity Price Risks—Alcoa is a leading global producer of aluminum ingot and aluminum fabricated products. As a condition of sale, customers often require Alcoa to enter into long-term, fixed-price commitments. These commitments expose Alcoa to the risk of higher aluminum prices between the time the order is committed and the time that the order is shipped. Alcoa also sells aluminum products to third parties at then-current market prices and is exposed to the risk of lower market prices at the time of shipment. Alcoa uses futures and options contracts, totaling approximately 560,000 mt at December 31, 2005, to reduce the aluminum price risk associated with a portion of these fixed-price firm commitments. The effects of this hedging activity will be recognized in earnings over the designated hedge periods, generally within three years.

Alcoa has also entered into options contracts, totaling approximately 150,000 mt at December 31, 2005, to hedge a portion of future production. The effect of this hedging activity will be recognized in earnings over the designated hedge periods in 2007 and 2008.

Alcoa has also entered into futures contracts to minimize its price risk related to other customer sales and pricing arrangements. Alcoa has not qualified these contracts for hedge accounting treatment, and therefore, the fair value gains and losses on these contracts are recorded in earnings. These contracts totaled 23,000 mt at December 31, 2005.

In addition, Alcoa has power supply contracts that contain pricing provisions related to the LME aluminum price. The LME-linked pricing features are considered embedded derivatives. A majority of these embedded derivatives have been designated as hedges of future sales of aluminum. Gains and losses on the remainder of these embedded derivatives are recognized in earnings.

The mark-to-market earnings impact from aluminum derivative and hedging activities was a loss of $11 in 2005. The loss was principally due to a loss of $21 for an embedded derivative in a power contract that was offset by gains of $11 for the ineffective portion of aluminum hedge contracts.

Alcoa purchases natural gas, fuel oil, and electricity to meet its production requirements and believes it is highly likely that

such purchases will continue in the future. These purchases expose the company to the risk of higher prices. To hedge a portion of these risks, Alcoa uses futures and forward contracts. The effects of this hedging activity will be recognized in earnings over the designated hedge periods, generally within three years.

Financial Risk

Interest Rates—Alcoa uses interest rate swaps to help maintain a strategic balance between fixed- and floating-rate debt and to manage overall financing costs. For a portion of its fixed-rate debt, the company has entered into pay floating, receive fixed interest rate swaps to effectively change the fixed interest rates to floating interest rates.

Currencies—Alcoa is subject to exposure from fluctuations in foreign currency exchange rates. Foreign currency exchange contracts may be used from time to time to hedge the variability in cash flows from the forecasted payment or receipt of
currencies other than the functional currency. These contracts cover periods consistent with known or expected exposures, generally within three years.

Fair Values and Sensitivity Analysis—The following table shows the fair values of outstanding derivative contracts at December 31, 2005 and the effect on fair values of a hypothetical change (increase or decrease of 10%) in the market prices or rates that existed at December 31, 2005.

	Fair value gain/(loss)	Index change of + / - 10%
Aluminum	$ 4	$ 119
Interest rates	(100)	65
Other commodities, principally natural gas	201	80
Currencies	83	4

Aluminum consists of hedge contracts with gains of $245. This is mostly offset by losses on embedded derivatives in power contracts in Iceland and Brazil and our share of losses on hedge contracts of Norwegian smelters that are accounted for under the equity method.

Material Limitations—The disclosures with respect to commodity prices, interest rates, and foreign exchange risk do not take into account the underlying commitments or anticipated transactions. If the underlying items were included in the analysis, the gains or losses on the futures contracts may be offset. Actual results will be determined by a number of factors that are not under Alcoa's control and could vary significantly from those factors disclosed.

Alcoa is exposed to credit loss in the event of nonperformance by counterparties on the above instruments, as well as credit or performance risk with respect to its hedged customers' commitments. Although nonperformance is possible, Alcoa does not anticipate nonperformance by any of these parties. Contracts are with creditworthy counterparties and are further supported by cash, treasury bills, or irrevocable letters of credit issued by carefully chosen banks. In addition, various master netting arrangements are in place with counterparties to facilitate settlement of gains and losses on these contracts.

For additional information on derivative instruments, see Notes A, K, and X to the Consolidated Financial Statements.

Environmental Matters

Alcoa continues to participate in environmental assessments and cleanups at a number of locations. These include approximately 35 owned or operating facilities and adjoining properties, approximately 33 previously owned or operating facilities and adjoining properties, and approximately 61 waste sites, including Superfund sites. A liability is recorded for environmental remediation costs or damages when a cleanup program becomes probable and the costs or damages can be reasonably estimated. See Note A for additional information.

As assessments and cleanups proceed, the liability is adjusted based on progress made in determining the extent of remedial actions and related costs and damages. The liability can change substantially due to factors such as the nature and extent of contamination, changes in remedial requirements, and technological changes. Therefore, it is not possible to determine the outcomes or to estimate with any degree of accuracy the potential costs for certain of these matters.

The following discussion provides additional details regarding the current status of Alcoa's significant sites where the final outcome cannot be determined or the potential costs in the future cannot be estimated.

Massena, NY—Alcoa has been conducting investigations and studies of the Grasse River, adjacent to Alcoa's Massena, NY plant site, under order from the U.S. Environmental Protection Agency (EPA) issued under the Comprehensive Environmental Response, Compensation and Liability Act, also known as Superfund. Sediments and fish in the river contain varying levels of polychlorinated biphenyl (PCB).

In 2002, Alcoa submitted an Analysis of Alternatives Report that detailed a variety of remedial alternatives with estimated costs ranging from $2 to $525. Because the selection of the $2 alternative (natural recovery) was considered remote, Alcoa adjusted the reserve for the Grasse River in 2002 to $30, representing the low end of the range of possible alternatives, as no single alternative could be identified as more probable than the others.

In June of 2003, based on river observations during the spring of 2003, the EPA requested that Alcoa gather additional field data to assess the potential for sediment erosion from winter river ice formation and breakup. The results of these additional studies, submitted in a report to the EPA in April of 2004, suggest that this phenomenon has the potential to occur approximately every 10 years and may impact sediments in certain portions of the river under all remedial scenarios. The EPA informed Alcoa that a final remedial decision for the river could not be made without substantially more information, including river pilot studies on the effects of ice formation and breakup on each of the remedial techniques. Alcoa submitted to EPA and EPA approved a Remedial Options Pilot Study (ROPS) to gather this information. The scope of this study includes sediment removal and capping, the installation of an ice control structure, and significant monitoring.

In May of 2004, Alcoa agreed to perform the study at an estimated cost of $35. Most of the construction work was completed in 2005 with monitoring proposed for 2006. The findings will be incorporated into a revised Analysis of Alternatives Report, which is expected to be submitted in 2007. This information will be used by the EPA to propose a remedy for the entire river.

Alcoa adjusted the reserves in the second quarter of 2004 to include the $35 for the ROPS. This was in addition to the $30 previously reserved. With the exception of the natural recovery remedy, none of the existing alternatives in the 2002 Analysis of Alternatives Report is more probable than the others, and the results of the ROPS are necessary to revise the scope and estimated cost of many of the current alternatives.

The EPA's ultimate selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA's Record of Decision is issued, which is expected in 2008 or later.

Sherwin, TX—In connection with the sale of the Sherwin alumina refinery in Texas, which was required to be divested as part of the Reynolds merger in 2000, Alcoa has agreed to retain responsibility for the remediation of then-existing environmental conditions, as well as a pro rata share of the final closure of the active waste disposal areas, which remain in use. Alcoa's share of the closure costs is proportional to the total period of operation of the active waste disposal areas. Alcoa estimated its liability for the active disposal areas by making certain assumptions about the period of operation, the amount of material placed in the area prior to closure, and the appropriate technology, engineering, and regulatory status applicable to final closure. The most probable cost for remediation has been reserved. It is reasonably possible that an additional liability, not expected to exceed $75, may be incurred if actual experience varies from the original assumptions used.

East St. Louis, IL—In response to questions regarding environmental conditions at the former East St. Louis, IL operations, Alcoa entered into an administrative order with the EPA in December 2002 to perform a remedial investigation and feasibility study of an area used for the disposal of bauxite residue from historic alumina refining operations. A draft feasibility study was submitted to the EPA in April 2005. The feasibility study includes remedial alternatives that range from no further action at $0 to significant grading, stabilization, and water management of the bauxite residue disposal areas at $75. Because the selection of the $0 alternative was considered remote, Alcoa increased the environmental reserve for this location by $15 in the second quarter of 2005, representing the low end of the range of possible alternatives which meets the remedy selection criteria, as no alternative could be identified as more probable than the others. The EPA has not completed a final review of the feasibility study, and the EPA's selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA's Record of Decision is issued.

Based on the foregoing, it is possible that Alcoa's results of operations, in a particular period, could be materially affected by matters relating to these sites. However, based on facts currently available, management believes that adequate reserves have been provided and that the disposition of these matters will not have a materially adverse effect on the financial position or liquidity of the company.

Alcoa's remediation reserve balance at the end of 2005 and 2004 was $390 and $391 (of which $40 and $73 were classified as a current liability), respectively, and reflects the most probable costs to remediate identified environmental conditions for which costs can be reasonably estimated. Remediation expenses charged to the reserve were approximately $53 in 2005, $46 in 2004, and $32 in 2003. These amounts include expenditures currently mandated, as well as those not required by any regulatory authority or third party. The reserve balance was increased by $52 in 2005, primarily due to the reserve recorded for the acquired Russian fabricating facilities in the first quarter and for the East St. Louis, IL facility which was recorded in the second quarter of 2005. In 2004, the reserve increased by $42, primarily for the additional reserve recorded for the Grasse River site.

Included in annual operating expenses are the recurring costs of managing hazardous substances and environmental programs. These costs are estimated to be about 2% of cost of goods sold.

Liquidity and Capital Resources

Alcoa takes a disciplined approach to cash management and strengthening its balance sheet, as it undertook aggressive capital controls, management of working capital, continued monitoring of growth projects, and continued focus on divestitures in 2005. Capital spending increased 87%, as Alcoa made continued progress on brownfield expansions in refining and smelting and continued construction on the greenfield smelter project in Iceland.

Cash provided from operations and from financing activities is anticipated to be adequate to cover dividends, debt repayments, capital expenditures, and other business needs over the next 12 months.

Cash from Operations

Cash from operations in 2005 was $1,676 compared with $2,199 in 2004. The decrease of $523, or 24%, was principally due to increases in receivables and inventories of $440 due to increased sales and higher prices; $282 increase in pension contributions in 2005; a reduction in tax liabilities of $222; and the payment of $93 associated with the long-term aluminum supply contract entered into as part of the acquisition of two Russian fabricating facilities. These items were partially offset by an increase in accounts payable and accrued expenses of $553 due to increased raw materials costs and increased payment terms.

Cash from operations in 2004 was $2,199 compared with $2,434 in 2003. The decrease of $235, or 10%, was principally due to increases in inventories due to higher metal prices and the absence of proceeds from a $440 advance payment against a long-term aluminum supply contract that occurred in 2003. Partially offsetting these items were stronger earnings in 2004 compared with 2003 and an increase in taxes payable and accounts payable. See the Results of Operations discussion for further details.

Financing Activities

Cash used for financing activities was $324 in 2005 compared with $1,525 in 2004. The change of $1,201 was primarily due to net debt repayments of $898 in 2004 compared with net borrowings of $311 in 2005.

Cash used for financing activities was $1,525 in 2004 compared with $1,714 in 2003. The change of $189 was primarily due to an increase in short-term borrowings related to accounts payable arrangements.

Alcoa maintains $3,000 of revolving-credit agreements with varying expiration dates as backup to its commercial paper program. In April 2005, Alcoa refinanced its $1,000 revolving-credit agreement that was to expire in April 2005 into a new $1,000 revolving-credit agreement that will expire in April 2010. Alcoa also has a $1,000 revolving-credit agreement that will expire in April 2008 and a $1,000 revolving-credit agreement that will expire in April 2009. Under these agreements, a certain ratio of indebtedness to consolidated net worth must be maintained. There were no amounts outstanding under the revolving-credit agreements at December 31, 2005. The interest rate on the agreements expiring in 2008 and 2009, if drawn upon, is Libor plus 17 basis points, which is subject to adjustment if Alcoa's credit rating changes, to a maximum interest rate of Libor plus 83.5 basis points. The interest rate on the agreement expiring in 2010 is Libor plus 18 basis points, which is subject to adjustment if Alcoa's credit rating changes, to a maximum interest rate of Libor plus 60 basis points. Alcoa had $3,000 of available borrowings at December 31, 2005. Debt of $58 will mature in 2006.

Standard and Poor's Rating Services' (S&P) long-term debt rating of Alcoa is A- and its short-term rating is A-2. The current outlook, which was revised in January 2005, is negative, as S&P cited higher capital expenditures in 2005 and future years. Moody's Investors Service long-term debt rating of Alcoa and its rated subsidiaries is A2, and its short-term debt rating of Alcoa is Prime-1.

Investing Activities

Cash used for investing activities was $1,035 in 2005 compared with $802 in 2004, resulting in a change of $233. The increase was primarily caused by an increase in capital expenditures of $995 as Alcoa continued to invest in growth projects, including alumina and smelting expansions and the greenfield smelter construction in Iceland. Cash paid for acquisitions of $262 related to the acquisition of two Russian facilities, and cash paid of $199 for the acquisition of minority interests was primarily related to AFL. These increases were largely offset by proceeds from the sale of investments of $1,081, including $869 from the sale of Alcoa's stake in Elkem ASA and $205 from the sale of Alcoa's interest in Integris Metals in 2005, and a $113 increase in the proceeds from the sale of assets and businesses, principally due to the $408 cash proceeds from the sale of the Southern Graphic Systems, Inc. business in 2005.

Cash used for investing activities was $802 in 2004 compared with $526 in 2003, resulting in a change of $276. The increase was caused primarily by an increase in capital spending of $273 as Alcoa invested in alumina and smelting expansions, as well as the greenfield smelter construction in Iceland in 2004. Cash proceeds from the sale of assets and businesses were $228 higher in 2004, due to the substantial completion of the company's 2002 divestiture plan, partially offset by a $129 decrease in cash received on the sale of investments.

Capital expenditures were $2,138 in 2005 compared with $1,143 and $870 in 2004 and 2003, respectively. Of the total capital expenditures in 2005, approximately 60% related to growth projects, including the construction of the Iceland smelter, the investment in the Mosjøen anode facility, the expansion of the Alumar smelter, and the alumina refinery expansions in Jamaica, Australia, and Brazil. Also included are costs related to environmental control in new and expanded facilities totaling $95 in 2005, $70 in 2004, and $37 in 2003. Total capital expenditures are anticipated to be in the range of $2,500 to $3,000 in 2006.

Alcoa added $30, $69, and $11 to its investments in 2005, 2004, and 2003, respectively. In 2005, Alcoa invested an additional $19 in the Dampier to Bunbury Natural Gas Pipeline in Western Australia. In 2004, Alcoa paid $32 to acquire approximately 44 million additional shares of Chalco to maintain its 8% ownership interest.

For a discussion of long-term liquidity, see the disclosure included in Contractual Obligations and Off-Balance Sheet Arrangements that follows.

Critical Accounting Policies and Estimates

The preparation of the financial statements in accordance with generally accepted accounting principles requires management to make judgments, estimates, and assumptions regarding uncertainties that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses. Areas that require significant judgments, estimates, and assumptions include the accounting for derivatives; environmental matters; asset retirement obligations; the testing of goodwill and other intangible assets for impairment; the impairment of properties, plants, and equipment; estimated proceeds on businesses to be divested; pensions and other postretirement benefits; and tax matters.

Management uses historical experience and all available information to make these judgments and estimates, and actual results will inevitably differ from those estimates and assumptions that are used to prepare the company's financial statements at any given time. Despite these inherent limitations, management believes that Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) and the financial statements and related footnotes provide a meaningful and fair perspective of the company. A discussion of the judgments and uncertainties associated with accounting for derivatives and environmental matters can be found in the Market Risks and Derivative Activities and the Environmental Matters sections of MD&A.

A summary of the company's significant accounting policies is included in Note A to the Consolidated Financial Statements. Management believes that the application of these policies on a consistent basis enables the company to provide the users of the financial statements with useful and reliable information about the company's operating results and financial condition.

Goodwill and indefinite-lived intangible assets are tested annually for impairment and whenever events or circumstances change, such as a significant adverse change in business climate or the decision to sell a business, that would make it more likely than not that an impairment may have occurred. The evaluation of impairment involves comparing the current fair value of each reporting unit to the recorded value, including goodwill. Alcoa uses a discounted cash flow model (DCF model) to determine the current fair value of its reporting units. A number of significant assumptions and estimates are involved in the application of the DCF model to forecast operating cash flows, including markets and market share, sales volumes and prices, costs to produce, and working capital changes. Management considers historical experience and all available information at the time the fair values of its reporting units are estimated. However, fair values that could be realized in an actual transaction may differ from those used to evaluate the impairment of goodwill.

Properties, plants, and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets (asset group) may not be recoverable. Recoverability of assets is determined by comparing the estimated undiscounted net cash flows of the operations to which the assets (asset group) related to their carrying amount. An impairment loss would be recognized when the carrying amount of the assets (asset group) exceeds the estimated undiscounted net cash flows. The amount of the impairment loss to be recorded is calculated as the excess of the carrying value of the assets (asset group) over their fair value, with fair value generally determined using a discounted cash flow analysis.

The fair values of all businesses to be divested are estimated using accepted valuation techniques such as a DCF model, earnings multiples, or indicative bids, when available. A number of significant estimates and assumptions are involved in the application of these techniques, including the forecasting of markets and market share, sales volumes and prices, costs and expenses, and multiple other factors. Management considers historical experience and all available information at the time the estimates are made; however, the fair values that are ultimately realized upon the sale of the businesses to be divested may differ from the estimated fair values reflected in the financial statements.

Other areas of significant judgments and estimates include the liabilities and expenses for pensions and other postretirement benefits. These amounts are determined using actuarial methodologies and incorporate significant assumptions, including the rate used to discount the future estimated liability, the long-term rate of return on plan assets, and several assumptions relating to the employee workforce (salary increases, medical costs, retirement age, and mortality). The rate used to discount future estimated liabilities is determined considering the rates available at year-end on debt instruments that could be used to settle the obligations of the plan. The impact on the liabilities of a change in the discount rate of 1/4 of 1% is approximately $390 and a charge or credit of $19 to after-tax earnings in the following year. The long-term rate of return is estimated by considering historical returns and expected returns on current and projected asset allocations and is generally applied to a five-year average market value of assets. A change in the assumption for the long-term rate of return on plan assets of 1/4 of 1% would impact after-tax earnings by approximately $14 for 2006. The 10-year moving average of actual performance has consistently exceeded 9% over the past 20 years.

In 2003, a net charge of $39 was recorded in shareholders' equity as strong asset returns of 19.75% almost entirely offset higher accumulated benefit obligations resulting from a 50 basis point decline in the discount rate. A net charge of $21 in shareholders' equity in 2004 reflected asset returns of 12%, which were more than offset by higher accumulated benefit obligations caused by a 25 basis point decline in the discount rate. In 2005, a net charge of $148 was recorded in shareholders' equity as asset returns of 8% were more than offset by higher accumulated benefit obligations caused by a 30 basis point decline in the discount rate.

As a global company, Alcoa records an estimated liability for income and other taxes based on what it determines will likely be paid in the various tax jurisdictions in which it operates.

Management uses its best judgment in the determination of these amounts. However, the liabilities ultimately incurred and paid are dependent on various matters, including the resolution of tax audits in the various affected tax jurisdictions, and may differ from the amounts recorded. An adjustment to the estimated liability would be recorded through income in the period in which it becomes probable that the amount of the actual liability differs from the amount recorded. Alcoa has unamortized tax-deductible goodwill of $507 resulting from intercompany stock sales and reorganizations (generally at a 34% rate). Alcoa recognizes the tax benefits associated with this tax-deductible goodwill as it is being amortized for local income tax purposes from 2004 through 2009, rather than in the period in which the transaction was consummated.

Related Party Transactions

Alcoa buys products from and sells products to various related companies, consisting of entities in which Alcoa retains a 50% or less equity interest, at negotiated arms-length prices between the two parties. These transactions were not material to the financial position or results of operations of Alcoa at December 31, 2005.

Recently Adopted Accounting Standards

Alcoa adopted FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" (FIN 47), effective December 31, 2005. See Note C to the Consolidated Financial Statements for additional information.

Recently Issued Accounting Standards

In December 2004, the FASB issued SFAS No. 123 (revised 2004) "Share-Based Payment." This standard requires companies to measure and recognize the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value. Alcoa will begin expensing stock options in the first quarter of 2006, using the modified prospective application. In addition, the company is required to reflect compensation expense for these individuals using the non-substantive vesting period approach, in which the compensation expense is recognized ratably over the requisite service period following the date of grant.

SFAS No. 154, "Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3," was issued in June 2005. SFAS No. 154 requires retrospective application to financial statements of prior periods for changes in accounting principle that are not adopted prospectively. This statement is effective January 1, 2006. This standard has no impact on Alcoa's 2005 financial statements.

SFAS No. 153, "Exchanges of Nonmonetary Assets—an amendment of APB Opinion No. 29," was issued in December 2004. This standard eliminates the exception for nonmonetary exchanges of similar productive assets to be measured based on the fair value of the assets exchanged and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. This standard is effective January 1, 2006. This standard has no impact on Alcoa's 2005 financial statements.

In 2005, the FASB issued Emerging Issues Task Force (EITF) Issue No. 04-6, "Accounting for Stripping Costs Incurred during Production in the Mining Industry." EITF 04-6 requires that stripping costs incurred during the production phase of a mine are to be accounted for as variable production costs that should be included in the costs of the inventory produced (that is, extracted) during the period that the stripping costs are incurred. EITF 04-6 is effective for the first reporting period in fiscal years beginning after December 15, 2005. Alcoa is currently evaluating the impact of this statement on the company.

Contractual Obligations and Off-Balance Sheet Arrangements

The company is obligated to make future payments under various contracts such as long-term purchase obligations, debt agreements, lease agreements, and unconditional purchase obligations and has certain commitments such as debt guarantees. The company has grouped these contractual obligations and off-balance sheet arrangements into operating activities, financing activities, and investing activities in the same manner as they are classified in the Statement of Consolidated Cash Flows in order to provide a better understanding of the nature of the obligations and arrangements and to provide a basis for comparison to historical information. The table below provides a summary of contractual obligations and off-balance sheet arrangements as of December 31, 2005:

Contractual obligations	Total	2006	2007-2008	2009-2010	Thereafter
Operating activities:					
Energy-related purchase obligations	$9,934	$ 800	$1,507	$1,224	$ 6,403
Raw material and other purchase obligations	2,340	1,509	634	102	95
Operating leases [1]	1,021	214	307	227	273
Estimated minimum required pension funding	[2]	154	800	250	[2]
Postretirement benefit payments	[2]	352	700	700	[2]
Layoff and other restructuring payments [3]	174	174	—	—	—
Deferred revenue arrangements	422	81	163	55	123
Financing activities:					
Total debt [4]	6,549	1,270	1,138	1,040	3,101
Dividends to shareholders [5]					
Investing activities:					
Capital projects [6]	4,410	2,750	1,590	70	—
Payments related to acquisitions [7]	142	115	27	—	—
Other:					
Standby letters of credit [8]	501	267	23	8	203
Guarantees [8]	431	1	15	19	396
Total contractual obligations		$7,687	$6,904	$3,695	

[1]See Note U to the Consolidated Financial Statements for further details on operating leases.
[2]Annual payments and funding are expected to continue into the foreseeable future at the amounts or ranges noted in the discussion that follows.
[3]See Note D to the Consolidated Financial Statements for further details on layoff and other restructuring payments.
[4]See Note K to the Consolidated Financial Statements for further details on debt and associated interest.
[5]See discussion that follows under Obligations for Financing Activities.
[6]See discussion that follows under Obligations for Investing Activities.
[7]See Note F to the Consolidated Financial Statements for further details on required payments related to acquisitions.
[8]See Note N to the Consolidated Financial Statements for further details on standby letters of credit and guarantees.

Obligations for Operating Activities

The table provides a summary of the type or nature of the company's obligations associated with operating activities that exceed $5 annually or $10 in total over the life of the contract. Energy-related purchase obligations consist primarily of electricity and natural gas contracts with expiration dates ranging from less than one year to 40 years. The majority of raw material and other purchase obligations have expiration dates of 24 months or less. Operating leases represent multi-year obligations for rental of facilities and equipment.

Estimated minimum required pension funding and postretirement benefit payments are based on actuarial estimates using current assumptions for discount rates, expected return on long-term assets, rate of compensation increases, and health care cost trend rates. The minimum required cash outlays for pension funding are estimated to be $154 for 2006 and $350 for 2007. The increase in 2007 is a result of the depletion of prior pension-funding credits that are projected to be fully used during 2006, requiring additional funding in 2007. The funding estimate for 2008 is $450, and the estimate for 2009 and 2010 is $250. Postretirement benefit payments are expected to approximate $350 annually. Annual payments will vary based on actuarial estimates. See Note W to the Consolidated Financial Statements for additional information.

Deferred revenue arrangements require Alcoa to deliver aluminum and alumina over the specified contract period. While these obligations are not expected to result in cash payments, they represent contractual obligations for which the company would be obligated if the specified product deliveries could not be made.

Obligations for Financing Activities

Cash outlays for financing activities consist primarily of debt and dividend payments to shareholders. The company has historically paid quarterly dividends to shareholders. Shareholder dividends are subject to quarterly approval by the company's Board of Directors and are currently at a rate of $524 annually.

Obligations for Investing Activities

Alcoa has made announcements indicating its participation in several significant expansion projects. These projects include the construction of a smelter in Iceland; the construction of an anode facility in Mosjøen, Norway; the expansion of alumina refineries at São Luis, Brazil; Pinjarra, Australia; and Clarendon, Jamaica. In addition, Alcoa announced its intention to participate in the construction of a smelter in Trinidad; a smelter joint venture project in China; and the investment in several hydroelectric power construction projects in Brazil. These projects are in various stages of development and, depending on business and/or regulatory circumstances, may not be completed. The amounts included in the preceding table for capital projects represent the amounts which have been approved by management for these projects as of December 31, 2005. Funding levels vary in future years based on anticipated construction schedules of the projects.

It is anticipated that significant expansion projects will be funded through various sources, including cash provided from operations. Alcoa anticipates that financing required to execute all of these investments will be readily available over the time frame required.

Management's Reports to Alcoa Shareholders

Management's Report on Financial Statements and Practices

The accompanying consolidated financial statements of Alcoa Inc. and its subsidiaries (the "Company") were prepared by management, which is responsible for their integrity and objectivity. The statements were prepared in accordance with generally accepted accounting principles and include amounts that are based on management's best judgments and estimates. The other financial information included in the annual report is consistent with that in the financial statements.

Management also recognizes its responsibility for conducting the Company's affairs according to the highest standards of personal and corporate conduct. This responsibility is characterized and reflected in key policy statements issued from time to time regarding, among other things, conduct of its business activities within the laws of the host countries in which the Company operates and potentially conflicting outside business interests of its employees. The Company maintains a systematic program to assess compliance with these policies.

Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. In order to evaluate the effectiveness of internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act, management has conducted an assessment, including testing, using the criteria in *Internal Control–Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's system of internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. The Company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management has excluded two facilities in the Russian Federation (the "Russian Facilities") and the Alcoa Bohai Aluminum Industries Company Limited joint venture from its assessment of internal control over financial reporting as of December 31, 2005 because they were acquired by the Company in purchase business combinations in 2005. The Russian Facilities and Alcoa Bohai Aluminum Industries Company Limited joint venture are majority-owned subsidiaries of the Company that represent, on a combined basis, 2% of consolidated total assets and 2% of consolidated revenue as of and for the year ended December 31, 2005.

Based on the assessment, management has concluded that the Company maintained effective internal control over financial reporting as of December 31, 2005, based on criteria in *Internal Control–Integrated Framework* issued by the COSO. Management's assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2005, has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which is included herein.

Management's Certifications

The certifications of the Company's Chief Executive Officer and Chief Financial Officer required by the Sarbanes-Oxley Act have been included as Exhibits 31 and 32 in the Company's Form 10-K. In addition, in 2005, the Company's Chief Executive Officer provided to the New York Stock Exchange the annual CEO certification regarding the Company's compliance with the New York Stock Exchange's corporate governance listing standards.

/s/ Alain J. P. Belda
Alain J. P. Belda
Chairman and
Chief Executive Officer

/s/ Joseph C. Muscari
Joseph C. Muscari
Executive Vice President
and Chief Financial Officer

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of Alcoa Inc.:

We have completed integrated audits of Alcoa Inc.'s 2005 and 2004 consolidated financial statements and of its internal control over financial reporting as of December 31, 2005, and an audit of its 2003 consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

Consolidated financial statements

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of income, shareholders' equity and cash flows present fairly, in all material respects, the financial position of Alcoa Inc. and its subsidiaries (Alcoa) at December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2005 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of Alcoa's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note C to the consolidated financial statements, Alcoa changed its methods of accounting for conditional asset retirement obligations in 2005 and asset retirement obligations in 2003.

Internal control over financial reporting

Also, in our opinion, management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Alcoa maintained effective internal control over financial reporting as of December 31, 2005 based on criteria established in *Internal Control–Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), is fairly stated, in all material respects, based on those criteria. Furthermore, in our opinion, Alcoa maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control–Integrated Framework* issued by the COSO. Alcoa's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of Alcoa's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As described in Management's Report on Internal Control over Financial Reporting, management has excluded two facilities in the Russian Federation (the "Russian Facilities") and the Alcoa Bohai Aluminum Industries Company Limited joint venture from its assessment of internal control over financial reporting as of December 31, 2005 because these entities were acquired by Alcoa in purchase business combinations in 2005. We have also excluded the Russian Facilities and Alcoa Bohai Aluminum Industries Company Limited joint venture from our audit of internal control over financial reporting. The Russian Facilities and Alcoa Bohai Aluminum Industries Company Limited joint venture are majority-owned subsidiaries that represent, on a combined basis, 2% of consolidated total assets and 2% of consolidated revenue as of and for the year ended December 31, 2005.

/s/ PricewaterhouseCoopers LLP
Pittsburgh, Pennsylvania
February 17, 2006, except with respect to our opinion on the consolidated financial statements insofar as it relates to the effects of the discontinued operations discussed in Note B, as to which the date is January 15, 2007.

Statement of Consolidated Income

Alcoa and subsidiaries

(in millions, except per-share amounts)

For the year ended December 31	2005	2004	2003
Sales (Q)	$25,568	$22,609	$20,282
Cost of goods sold	20,704	17,928	16,114
Selling, general administrative, and other expenses	1,295	1,194	1,173
Research and development expenses	192	178	187
Provision for depreciation, depletion, and amortization	1,256	1,177	1,149
Restructuring and other charges (D)	292	(22)	(27)
Interest expense (V)	339	271	314
Other income, net (O)	(480)	(270)	(273)
	23,598	20,456	18,637
Income from continuing operations before taxes on income	1,970	2,153	1,645
Provision for taxes on income (T)	454	539	395
Income from continuing operations before minority interests' share	1,516	1,614	1,250
Less: Minority interests' share	259	245	238
Income from continuing operations	1,257	1,369	1,012
Loss from discontinued operations (B)	(22)	(59)	(27)
Cumulative effect of accounting changes (C)	(2)	—	(47)
Net Income	$ 1,233	$ 1,310	$ 938
Earnings (loss) per Share (S)			
Basic:			
Income from continuing operations	$ 1.44	$ 1.57	$ 1.18
Loss from discontinued operations	(.03)	(.07)	(.03)
Cumulative effect of accounting changes	—	—	(.06)
Net income	$ 1.41	$ 1.50	$ 1.09
Diluted:			
Income from continuing operations	$ 1.43	$ 1.56	$ 1.18
Loss from discontinued operations	(.03)	(.07)	(.04)
Cumulative effect of accounting changes	—	—	(.06)
Net income	$ 1.40	$ 1.49	$ 1.08

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Balance Sheet

(in millions)

December 31	2005	2004
Assets		
Current assets:		
Cash and cash equivalents (X)	$ 762	$ 457
Receivables from customers, less allowances: 2005—$75; 2004—$81	2,860	2,651
Other receivables	427	257
Inventories (G)	3,392	2,929
Fair value of derivative contracts	520	311
Prepaid expenses and other current assets	713	755
Total current assets	8,674	7,360
Properties, plants, and equipment, net (H)	13,108	12,222
Goodwill (E and F)	6,212	6,375
Investments (I)	1,370	2,066
Other assets (J)	4,084	3,819
Assets held for sale (B)	248	767
Total Assets	$33,696	$32,609
Liabilities		
Current liabilities:		
Short-term borrowings (K and X)	$ 300	$ 267
Commercial paper (K and X)	912	630
Accounts payable, trade	2,570	2,159
Accrued compensation and retirement costs	1,096	1,006
Taxes, including taxes on income	871	1,017
Other current liabilities	1,445	1,054
Long-term debt due within one year (K and X)	58	57
Total current liabilities	7,252	6,190
Long-term debt, less amount due within one year (K and X)	5,279	5,345
Accrued pension benefits (W)	1,500	1,513
Accrued postretirement benefits (W)	2,105	2,150
Other noncurrent liabilities and deferred credits (L)	1,821	1,725
Deferred income taxes (T)	875	789
Liabilities of operations held for sale (B)	126	181
Total liabilities	18,958	17,893
Minority interests (M)	1,365	1,416
Commitments and contingencies (N)		
Shareholders' Equity		
Preferred stock (R)	55	55
Common stock (R)	925	925
Additional capital	5,720	5,775
Retained earnings	9,345	8,636
Treasury stock, at cost	(1,899)	(1,926)
Accumulated other comprehensive loss	(773)	(165)
Total shareholders' equity	13,373	13,300
Total Liabilities and Equity	$33,696	$32,609

The accompanying notes are an integral part of the consolidated financial statements.

Statement of Consolidated Cash Flows

(in millions)

Alcoa and subsidiaries

For the year ended December 31	2005	2004	2003
Cash from Operations			
Net income	$ 1,233	$ 1,310	$ 938
Adjustments to reconcile net income to cash from operations:			
Depreciation, depletion, and amortization	1,258	1,185	1,158
Deferred income taxes	(16)	(95)	128
Equity loss (income), net of dividends	35	(54)	(94)
Restructuring and other charges (D)	292	(22)	(27)
Net gain on early retirement of debt and interest rate swap settlements (K and O)	—	(58)	—
Gains from investing activities—sale of assets and businesses (O)	(406)	(44)	(37)
Provision for doubtful accounts	19	24	11
Loss from discontinued operations (B)	22	59	27
Accounting changes (C)	2	—	47
Minority interests	259	245	238
Other	30	80	116
Changes in assets and liabilities, excluding effects of acquisitions and divestitures:			
Increase in receivables	(469)	(130)	(111)
(Increase) reduction in inventories	(503)	(402)	94
(Increase) reduction in prepaid expenses and other current assets	(3)	(94)	54
Increase (reduction) in accounts payable and accrued expenses	663	110	(171)
(Reduction) increase in taxes, including taxes on income	(102)	120	(247)
Cash paid on early retirement of debt and interest rate swap settlements (K)	—	(52)	—
Cash (paid) received on long-term aluminum supply contract	(93)	—	440
Pension contributions	(383)	(101)	(87)
Net change in other noncurrent assets and liabilities	(194)	(134)	(146)
Reduction in net assets held for sale	—	185	30
Cash provided from continuing operations	1,644	2,132	2,361
Cash provided from discontinued operations	32	67	73
Cash from operations	1,676	2,199	2,434
Financing Activities			
Net changes to short-term borrowings	5	213	12
Common stock issued for stock compensation plans	72	83	98
Repurchase of common stock	(108)	(67)	—
Dividends paid to shareholders	(524)	(524)	(516)
Dividends paid to minority interests	(75)	(119)	(207)
Net change in commercial paper	282	630	(665)
Additions to long-term debt	278	180	387
Payments on long-term debt	(254)	(1,921)	(823)
Cash used for financing activities	(324)	(1,525)	(1,714)
Investing Activities			
Capital expenditures	(2,116)	(1,137)	(857)
Capital expenditures of discontinued operations	(22)	(6)	(13)
Acquisition of minority interests (F and P)	(199)	—	—
Acquisitions, net of cash acquired (F and P)	(262)	(2)	(9)
Proceeds from the sale of assets and businesses	505	392	164
Additions to investments	(30)	(69)	(11)
Sale of investments (F)	1,081	—	129
Changes in short-term investments	(8)	30	19
Other	16	(10)	52
Cash used for investing activities	(1,035)	(802)	(526)
Effect of exchange rate changes on cash	(12)	9	38
Net change in cash and cash equivalents	305	(119)	232
Cash and cash equivalents at beginning of year	457	576	344
Cash and cash equivalents at end of year	$ 762	$ 457	$ 576

The accompanying notes are an integral part of the consolidated financial statements.

Statement of Shareholders' Equity

(in millions, except per-share amounts)

December 31	Comprehensive income	Preferred stock	Common stock	Additional capital	Retained earnings	Treasury stock	Accumulated other compre- hensive loss	Total shareholders' equity
Balance at end of 2002		$ 55	$ 925	$ 6,101†	$ 7,428	$ (2,828)	$ (1,754)	$ 9,927
Comprehensive income—2003:								
Net income—2003	$ 938				938			938
Other comprehensive income (loss):								
Change in minimum pension liability, net of $21 tax benefit	(39)							
Currency translation adjustments	818							
Unrealized gains on available-for-sale securities, net of $183 tax expense	340							
Unrecognized gains/(losses) on derivatives, net of tax and minority interests of $(53):								
Net change from periodic revaluations	115							
Net amount reclassified to income	(49)							
Net unrecognized gains on derivatives	66							
Comprehensive income	$ 2,123						1,185	1,185
Cash dividends: Preferred @ $3.75 per share					(2)			(2)
Common @ $.60 per share					(514)			(514)
Stock issued: Alcoa Alumínio minority interest acquisition (F)				(193)		603		410
Stock issued: compensation plans				(77)		208		131
Balance at end of 2003		55	925	5,831†	7,850	(2,017)	(569)	12,075
Comprehensive income—2004:								
Net income—2004	$ 1,310				1,310			1,310
Other comprehensive income (loss):								
Change in minimum pension liability, net of $11 tax benefit	(21)							
Currency translation adjustments	535							
Unrealized losses on available-for-sale securities, net of $51 tax benefit (X)	(94)							
Unrecognized gains/(losses) on derivatives, net of tax and minority interests of $34 (X):								
Net change from periodic revaluations	120							
Net amount reclassified to income	(136)							
Net unrecognized losses on derivatives	(16)							
Comprehensive income	$ 1,714						404	404
Cash dividends: Preferred @ $3.75 per share					(2)			(2)
Common @ $.60 per share					(522)			(522)
Stock issued: compensation plans				(56)		91		35
Balance at end of 2004		55	925	5,775†	8,636	(1,926)	(165)	13,300
Comprehensive income—2005:								
Net income—2005	$ 1,233				1,233			1,233
Other comprehensive income (loss):								
Change in minimum pension liability, net of $80 tax benefit	(148)							
Currency translation adjustments	(542)							
Unrealized gains on available-for-sale securities, net of $52 tax expense (X)	96							
Unrecognized gains/(losses) on derivatives, net of tax and minority interests of $87 (X):								
Net change from periodic revaluations	123							
Net amount reclassified to income	(137)							
Net unrecognized losses on derivatives	(14)							
Comprehensive income	$ 625						(608)	(608)
Cash dividends: Preferred @ $3.75 per share					(2)			(2)
Common @ $.60 per share					(522)			(522)
Stock issued: compensation plans				(55)		27		(28)
Balance at end of 2005		$ 55	$ 925	$ 5,720†	$ 9,345	$ (1,899)	$ (773)*	$ 13,373

* Comprised of unrealized translation adjustments of $(7), minimum pension liability of $(1,120), unrealized gains on available-for-sale securities of $317, and unrecognized gains/(losses) on derivatives of $37, net of tax

† Includes stock to be issued under options of $67 in 2005, $96 in 2004, $130 in 2003, and $130 in 2002

The accompanying notes are an integral part of the consolidated financial statements.

Notes to the Consolidated Financial Statements

(dollars in millions, except per-share amounts)

A. Summary of Significant Accounting Policies

Basis of Presentation. The Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America and require management to make certain estimates and assumptions. These may affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. They also may affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates upon subsequent resolution of identified matters.

Principles of Consolidation. The Consolidated Financial Statements include the accounts of Alcoa and companies in which Alcoa has a controlling interest. Intercompany transactions have been eliminated. The equity method of accounting is used for investments in affiliates and other joint ventures over which Alcoa has significant influence (ownership between twenty and fifty percent) but does not have effective control. Investments in affiliates in which Alcoa cannot exercise significant influence (ownership interest less than twenty percent) are accounted for on the cost method.

Alcoa also evaluates consolidation of entities under Financial Accounting Standards Board (FASB) Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 requires management to evaluate whether an entity or interest is a variable interest entity and whether Alcoa is the primary beneficiary. Consolidation is required if both of these criteria are met. Alcoa does not have any variable interest entities requiring consolidation.

Cash Equivalents. Cash equivalents are highly liquid investments purchased with an original maturity of three months or less.

Inventory Valuation. Inventories are carried at the lower of cost or market, with cost for a substantial portion of U.S. and Canadian inventories determined under the last-in, first-out (LIFO) method. The cost of other inventories is principally determined under the average-cost method. See Note G for additional information.

Properties, Plants, and Equipment. Properties, plants, and equipment are recorded at cost. Depreciation is recorded principally on the straight-line method at rates based on the estimated useful lives of the assets, averaging 33 years for structures and approximately 16 years for machinery and equipment, as useful lives range between 5 and 25 years. Gains or losses from the sale of assets are generally recorded in other income (see policy that follows for assets classified as held for sale and discontinued operations). Repairs and maintenance are charged to expense as incurred. Interest related to the construction of qualifying assets is capitalized as part of the construction costs. Depletion related to mineral reserves is recorded using the units of production method. See Notes H and V for additional information.

Properties, plants, and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets (asset group) may not be recoverable. Recoverability of assets is determined by comparing the estimated undiscounted net cash flows of the operations to which the assets (asset group) related to their carrying amount. An impairment loss would be recognized when the carrying amount of the assets (asset group) exceeds the estimated undiscounted net cash flows. The amount of the impairment loss to be recorded is calculated as the excess of the carrying value of the assets (asset group) over their fair value, with fair value generally determined using a discounted cash flow analysis.

Goodwill and Other Intangible Assets. Goodwill and intangibles with indefinite useful lives are not amortized. Intangible assets with finite useful lives are amortized generally on a straight-line basis over the periods benefited, with a weighted average useful life of 13 years.

Goodwill and indefinite-lived intangible assets are tested annually for impairment and whenever events or circumstances change, such as a significant adverse change in business climate or the decision to sell a business, that would make it more likely than not that an impairment may have occurred. If the carrying value of goodwill or an indefinite-lived intangible asset exceeds its fair value, an impairment loss is recognized. The evaluation of impairment involves comparing the current fair value of each of the reporting units to the recorded value, including goodwill. Alcoa uses a discounted cash flow model (DCF model) to determine the current fair value of its reporting units. A number of significant assumptions and estimates are involved in the application of the DCF model to forecast operating cash flows, including markets and market share, sales volumes and prices, costs to produce, and working capital changes. Management considers historical experience and all available information at the time the fair values of its reporting units are estimated. However, fair values that could be realized in an actual transaction may differ from those used to evaluate the impairment of goodwill. See Note E for additional information.

Accounts Payable Arrangements. Alcoa participates in computerized payable settlement arrangements with certain vendors and third-party intermediaries. The arrangements provide that, at the vendor's request, the third-party intermediary advances the amount of the scheduled payment to the vendor, less an appropriate discount, before the scheduled payment date. Alcoa makes payment to the third-party intermediary on the date stipulated in accordance with the commercial terms negotiated with its vendors. The amounts outstanding under these arrangements that will be paid through the third-party intermediaries are classified as short-term borrowings in the Consolidated Balance Sheet and as cash provided from financing activities in the Statement of Consolidated Cash Flows. Alcoa records imputed interest related to these arrangements as interest expense in the Statement of Consolidated Income. See Note K for additional information.

Revenue Recognition. Alcoa recognizes revenue when title, ownership, and risk of loss pass to the customer.

Alcoa periodically enters into long-term supply contracts with alumina and aluminum customers and receives advance payments for product to be delivered in future periods. These advance payments are recorded as deferred revenue, and revenue is recognized as shipments are made and title, ownership, and risk of loss pass to the customer during the term of the contracts.

Environmental Expenditures. Expenditures for current operations are expensed or capitalized, as appropriate. Expenditures relating to existing conditions caused by past operations, and which do not contribute to future revenues, are expensed. Liabilities are recorded when remedial efforts are probable and the costs can be reasonably estimated. The liability may include costs such as site investigations, consultant fees, feasibility studies, outside contractor, and monitoring expenses. Estimates are generally not discounted or reduced by potential claims for recovery. Claims for recovery are recognized as agreements are reached with third parties. The estimates also include costs related to other potentially responsible parties to the extent that Alcoa has reason to believe such parties will not fully pay their proportionate share. The liability is periodically reviewed and adjusted to reflect current remediation progress, prospective estimates of required activity, and other factors that may be relevant, including changes in technology or regulations. See Note Y for additional information.

Asset Retirement Obligations. Alcoa recognizes asset retirement obligations (AROs) related to legal obligations associated with the normal operation of Alcoa's bauxite mining, alumina refining, and aluminum smelting facilities. These AROs consist primarily of costs associated with spent pot lining disposal, closure of bauxite residue areas, mine reclamation, and landfill closure. Alcoa would also recognize an ARO for any significant lease restoration obligation if required by a lease agreement. The fair values of these AROs are recorded on a discounted basis, at the time the obligation is incurred, and accreted over time for the change in present value. Additionally, Alcoa capitalizes asset retirement costs by increasing the carrying amount of the related long-lived assets and depreciating these assets over the remaining useful life.

Income Taxes. The provision for income taxes is determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax bases of Alcoa's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized. Alcoa also has unamortized tax-deductible goodwill resulting from intercompany stock sales and reorganizations. Alcoa recognizes the tax benefits associated with this tax-deductible goodwill as it is being amortized for local income tax purposes rather than in the period in which the transaction is consummated.

Stock-Based Compensation. Alcoa accounts for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations using the intrinsic value method, which resulted in no compensation cost for options granted.

Alcoa's net income and earnings per share would have been reduced to the pro forma amounts shown below if compensation cost had been determined based on the fair value at the grant dates in accordance with Statement of Financial Accounting Standards (SFAS) Nos. 123 and 148, "Accounting for Stock-Based Compensation."

	2005	2004	2003
Net income, as reported	$1,233	$1,310	$ 938
Less: compensation cost determined under the fair value method, net of tax	63	35	30
Pro forma net income	$1,170	$1,275	$ 908
Basic net income per share:			
As reported	$ 1.41	$ 1.50	$1.09
Pro forma	1.34	1.46	1.06
Diluted net income per share:			
As reported	1.40	1.49	1.08
Pro forma	1.33	1.45	1.06

Alcoa currently discloses the pro forma and actual compensation expense related to retiree-eligible employees using the nominal vesting approach, in which the compensation expense is recognized ratably over the original vesting period. Upon adoption of SFAS No. 123 (revised 2004) "Share-Based Payment" (SFAS No. 123(R)), the company is required to recognize compensation expense for these employees using the non-substantive vesting period approach, in which the compensation expense is recognized ratably over the
requisite service period following the date of grant. The impact of this change on the attribution period would not have had a material impact on the results of operations for the periods presented herein.

On December 31, 2005, Alcoa accelerated the vesting of 11 million unvested stock options granted to employees in 2004 and on January 13, 2005. The 2004 and 2005 accelerated options have weighted average exercise prices of $35.60 and $29.54, respectively, and in the aggregate, represent approximately 12 percent of Alcoa's total outstanding options. The decision to accelerate the vesting of the 2004 and 2005 options was made primarily to avoid recognizing the related compensation cost in future financial statements upon the adoption of SFAS No. 123(R), which Alcoa will adopt on January 1, 2006. The accelerated vesting of the 2004 and 2005 stock options will reduce Alcoa's after-tax stock option compensation expense in 2006 by $21 and in 2007 by $7.

In addition to stock option awards described above, beginning in 2004 the company granted stock awards and performance share awards that vest in three years from the date of grant. Compensation expense is calculated based on the fair value at the grant dates, and the after-tax expense recognized on these awards in 2005 and 2004 was $16 and $9, respectively.

In anticipation of the adoption of SFAS No. 123(R), Alcoa switched from the Black-Scholes pricing model to a lattice model to estimate fair value at grant date for options granted in 2005. The financial impact of this change was not material. Alcoa will begin expensing options using the modified prospective application.

The fair value of each option is estimated on the date of grant or subsequent reload using the lattice or Black-Scholes pricing model, as applicable, with the following assumptions:

December 31	2005	2004	2003
Average risk-free interest rate	2.65-4.2%	2.1%	2.2%
Expected dividend yield	1.8	1.6	2.5
Expected volatility	27-35	32	38
Expected life (years):			
New option grants	3.8	3.0	3.0
Reload option grants	—	3.0	2.5
Exercise behavior assumption	32	—	—

The weighted average fair value per option granted was $6.18 in 2005, $7.72 in 2004, and $5.75 in 2003. See Note R for additional information.

Derivatives and Hedging. Derivatives are held as part of a formally documented risk management program. All derivatives are straightforward and are held for purposes other than trading. For derivatives designated as fair value hedges, Alcoa measures hedge effectiveness by formally assessing, at least quarterly, the historical high correlation of changes in the fair value of the hedged item and the derivative hedging instrument. For derivatives designated as cash flow hedges, Alcoa measures hedge effectiveness by formally assessing, at least quarterly, the probable high correlation of the expected future cash flows of the hedged item and the derivative hedging instrument. The ineffective portions of both types of hedges are recorded in revenues or other income or expense in the current period. A gain of $11 was recorded in 2005 (loss of $18 in 2004) for the ineffective portion of aluminum hedges. If the hedging relationship ceases to be highly effective or it becomes probable that an expected transaction will no longer occur, future gains or losses on the derivative are recorded in other income or expense. Two interest rate swaps ceased to qualify as hedges in 2004, due to the restructuring of debt, and were terminated. See Notes K and X for additional information. No other hedging transactions ceased to qualify as hedges in 2005 or 2004.

Alcoa accounts for interest rate swaps related to its existing long-term debt and hedges of firm customer commitments for aluminum as fair value hedges. As a result, the fair values of derivatives and changes in the fair values of the underlying hedged items are reported in other current and noncurrent assets and liabilities in the Consolidated Balance Sheet. Changes in the fair values of these derivatives and underlying hedged items generally offset and are recorded each period in sales or interest expense, consistent with the underlying hedged item.

Alcoa accounts for hedges of foreign currency exposures and certain forecasted transactions, principally purchases of natural gas, as cash flow hedges. The fair values of the derivatives are recorded in other current and noncurrent assets and liabilities in the Consolidated Balance Sheet. The effective portions of the changes in the fair values of these derivatives are recorded in other comprehensive income (a gain of $37 at December 31, 2005) and are reclassified to sales, cost of goods sold, or other income in the period in which earnings are impacted by the hedged items or in the period that the transaction no longer qualifies as a cash flow hedge. These contracts cover the same periods as known or expected exposures, generally within three years. Assuming market rates remain constant with the rates at December 31, 2005, a gain of $102 is expected to be recognized in earnings over the next 12 months.

If no hedging relationship is designated, the derivative is marked to market through earnings.

Cash flows from financial instruments are recognized in the Statement of Consolidated Cash Flows in a manner consistent with the underlying transactions. See Notes K and X for additional information.

Foreign Currency. The local currency is the functional currency for Alcoa's significant operations outside the U.S., except certain operations in Canada, where the U.S. dollar is used as the functional currency. The determination of the functional currency for Alcoa's operations is made based on the appropriate economic and management indicators.

Acquisitions. Alcoa's acquisitions are accounted for using the purchase method. The purchase price is allocated to the assets acquired and liabilities assumed based on their estimated fair market values. Any excess purchase price over the fair market value of the net assets acquired is recorded as goodwill. For all acquisitions, operating results are included in the Statement of Consolidated Income since the dates of the acquisitions. See Note F for additional information.

Discontinued Operations and Assets Held For Sale. For those businesses where management has committed to a plan to divest, each business is valued at the lower of its carrying amount or estimated fair value less cost to sell. If the carrying amount of the business exceeds its estimated fair value, a loss is recognized. The fair values are estimated using accepted valuation techniques such as a DCF model, earnings multiples, or indicative bids, when available. A number of significant estimates and assumptions are involved in the application of these techniques, including the forecasting of markets and market share, sales volumes and prices, costs and expenses, and multiple other factors. Management considers historical experience and all available information at the time the estimates are made; however, the fair values that are ultimately realized upon the sale of the businesses to be divested may differ from the estimated fair values reflected in the financial statements.

Businesses to be divested are classified in the Consolidated Financial Statements as either discontinued operations or assets held for sale. For businesses classified as discontinued operations, the balance sheet amounts and income statement results are reclassified from their historical presentation to assets and liabilities of operations held for sale on the Consolidated Balance Sheet and to discontinued operations in the Statement of Consolidated Income for all periods presented. The gains or losses associated with these divested businesses are recorded in income (loss) from discontinued operations in the Statement of Consolidated Income. The Statement of Consolidated Cash Flows is also reclassified for assets held for sale and discontinued operations for all periods presented. Additionally, segment information does not include the results of businesses classified as discontinued operations. Management does not expect any continuing involvement with these businesses following the sales, and these businesses are expected to be disposed of within one year.

For businesses classified as assets held for sale that do not qualify for discontinued operations treatment, the balance sheet and cash flow amounts are reclassified from their historical presentation to assets and liabilities of operations held for sale. The income statement results continue to be reported in the historical income statement categories as income from continuing operations. The gains or losses associated with these divested

businesses are generally recorded in restructuring and other charges in the Statement of Consolidated Income. The segment results include the results of businesses classified as assets held for sale for all periods presented. Management expects that Alcoa will have continuing involvement with these businesses following the sale, primarily in the form of ongoing aluminum or other significant supply contracts.

Recently Adopted Accounting Standards. Alcoa adopted FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" (FIN 47), effective December 31, 2005. See Note C for additional information.

Recently Issued Accounting Standards. SFAS No. 123 (revised 2004) "Share-Based Payment" was issued in December 2004. This standard requires companies to measure and recognize the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value. Alcoa will begin expensing stock options in the first quarter of 2006, using the modified prospective application. In addition, the company is required to reflect compensation expense for these individuals using the non-substantive vesting period approach, in which the compensation expense is recognized ratably over the requisite service period following the date of grant.

SFAS No. 154, "Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3," was issued in June 2005. SFAS No. 154 requires retrospective application to financial statements of prior periods for changes in accounting principle that are not adopted prospectively. This statement is effective January 1, 2006. This standard has no impact on Alcoa's 2005 financial statements.

SFAS No. 153, "Exchanges of Nonmonetary Assets—an amendment of APB Opinion No. 29," was issued in December 2004. This standard eliminates the exception for nonmonetary exchanges of similar productive assets to be measured based on the fair value of the assets exchanged and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. This standard is effective January 1, 2006. This standard has no impact on Alcoa's 2005 financial statements.

In 2005, the FASB issued Emerging Issues Task Force (EITF) Issue No. 04-6, "Accounting for Stripping Costs Incurred during Production in the Mining Industry." EITF 04-6 requires that stripping costs incurred during the production phase of a mine are to be accounted for as variable production costs that should be included in the costs of the inventory produced (that is, extracted) during the period that the stripping costs are incurred. EITF 04-6 is effective for the first reporting period in fiscal years beginning after December 15, 2005. Alcoa is currently evaluating the impact of this statement on the company.

Reclassification. Certain amounts in previously issued financial statements were reclassified to conform to 2005 presentations. See Note B for further information.

B. Discontinued Operations and Assets Held for Sale

In the third quarter of 2006, Alcoa reclassified its home exteriors business to discontinued operations upon the signing of a definitive sale agreement with Ply Gem Industries, Inc. In the first quarter of 2006, Alcoa reclassified the Hawesville, KY automotive casting facility to discontinued operations upon closure of the facility. The results of the Extruded and End Products segment and the Engineered Solutions segment have been reclassified to reflect the movement of the home exteriors business and the automotive casting facility, respectively, into discontinued operations. The consolidated financial statements for all periods presented have been reclassified to reflect these businesses in discontinued operations.

In the third quarter of 2005, Alcoa reclassified the imaging and graphic communications business of Southern Graphic Systems, Inc. to discontinued operations based on the decision to sell the business. The results of the Packaging and Consumer segment have been reclassified to reflect the movement of this business into discontinued operations. The sale was completed in the fourth quarter of 2005.

The divestitures of the following businesses were completed in 2005: the telecommunications business, the protective packaging business, and the imaging and graphic communications business. See Note F for additional details.

At the end of 2005, businesses classified as discontinued operations included the home exteriors business, the Hawesville, KY automotive casting facility, the wireless component of the telecommunications business and a small automotive casting business in the U.K.

The following table details selected financial information for the businesses included within discontinued operations in the Statement of Consolidated Income.

	2005	2004	2003
Sales	$1,033	$1,352	$1,446
Income from operations	$ 38	$ 37	$ 18
Gain on sale of businesses	50	8	—
Loss from impairment	(55)	(153)	(69)
Pretax income (loss)	33	(108)	(51)
(Provision)/benefit for taxes	(57)	6	17
Minority interests	2	43	7
Loss from discontinued operations	$ (22)	$ (59)	$ (27)

The loss of $22 in discontinued operations in 2005 was comprised of $21 in net operating income, offset by $43 of net losses associated with businesses impaired or sold in 2005, including a $28 loss for asset impairments associated with the Hawesville, KY automotive casting facility. The loss of $59 in discontinued operations in 2004 was comprised of impairment losses of $89 to reflect the estimated fair values of the protective packaging and telecommunications businesses, as well as the U.K. automotive casting business, somewhat offset by $25 of net operating income of these businesses and a net gain of $5 on businesses sold in 2004. The loss of $27 in discontinued operations in 2003 was comprised of an impairment loss of $45 related to a reduction in the estimated fair value of the automotive fasteners business, somewhat offset by $18 of operating income.

The major classes of assets and liabilities of operations held for sale in the Consolidated Balance Sheet are as follows:

December 31	2005	2004
Assets:		
Receivables	$ 78	$190
Inventories	61	83
Properties, plants, and equipment, net	63	187
Other assets	46	307
Total assets held for sale	$248	$767
Liabilities:		
Accounts payable, accrued expenses and other	$126	$181
Total liabilities of operations held for sale	$126	$181

For all of the businesses to be divested, the fair values were estimated utilizing accepted valuation techniques. The fair values that are ultimately realized upon the sale of the businesses to be divested may differ from the estimated fair values reflected in the financial statements.

C. Asset Retirement Obligations

Alcoa adopted FIN 47, effective December 31, 2005. FIN 47 clarifies the accounting for conditional asset retirement obligations (CAROs), as referenced in SFAS No. 143, "Accounting

for Asset Retirement Obligations." A CARO is a legal obligation to perform an asset retirement activity in which the obligation is unconditional, but uncertainty exists about the timing and/or method of settlement, which may or may not be under the control of Alcoa, and which prevents the reasonable estimation of the fair value of the CARO. Upon adoption, Alcoa recognized a cumulative effect adjustment of $2, consisting primarily of costs for regulated waste materials related to the demolition of certain power facilities. Pro forma amounts related to prior periods are not presented, as there is no impact on prior period financial statements.

Historically, Alcoa has either operated locations or sold them and, in certain circumstances, has curtailed them for possible future use while continuing with ongoing security, utility and other maintenance costs as deemed necessary. In the event of a decision to permanently shutdown and/or demolish a facility, Alcoa would record an ARO for the removal, treatment, transportation, storage and/or disposal of various regulated assets and hazardous materials such as asbestos, underground and aboveground storage tanks, PCBs, various process residuals, solid wastes, electronic equipment waste, and various other materials.

AROs have not been recorded in the financial statements for any Alcoa operating location—other than those with specific legal obligations for spent pot lining disposal, closure of bauxite residue areas, mine reclamation, landfill closure, and specific lease restoration requirements—because the fair value of such potential retirement obligations cannot be measured as the settlement dates for these operating locations cannot be estimated. Such amounts may be material to the financial statements in the period in which they are recorded.

Effective January 1, 2003, Alcoa adopted SFAS No. 143. The cumulative effect adjustment recognized upon adoption of this standard was $47, consisting primarily of costs to establish assets and liabilities related to spent pot lining disposal for pots currently in operation.

The following table details the changes in the carrying amount of AROs.

December 31	2005	2004
Balance at beginning of year	$233	$ 217
Accretion expense	14	15
Payments	(31)	(25)
Liabilities incurred	46	30
Translation and other	(4)	(4)
Balance at end of year	$258	$ 233

D. Restructuring and Other Charges

Restructuring and other charges for each of the three years in the period ended December 31, 2005, were comprised of:

	2005	2004	2003
Asset impairments	$ 86	$ 6	$ —
Layoff costs	238	40	44
Other costs	16	—	—
Gain on sale of specialty chemicals business	—	(53)	—
Net reversals of previously recorded layoff and other costs*	(48)	(15)	(38)
Net reversals of previously recorded gains/losses on assets held for sale	—	—	(33)
Restructuring and other charges	$292	$(22)	$(27)

*Reversals of previously recorded layoff and other costs resulted from changes in facts and circumstances that led to changes in estimated costs.

2005 Restructuring Program. As a result of the global realignment of Alcoa's organization structure, designed to optimize operations in order to better serve customers, a restructuring plan was developed to identify opportunities to streamline operations on a global basis. The restructuring program consisted of the elimination of jobs across all segments of the company, various plant closings and consolidations, and asset disposals. Restructuring charges of $292 ($190 after tax and minority interests) were recorded in 2005 and were comprised of the following components: $238 of charges for employee termination and severance costs associated with approximately 8,450 salaried and hourly employees, spread globally across the company; $86 related to asset impairments for structures, machinery, and equipment; and $16 for exit costs, consisting primarily of accelerated depreciation associated with assets for which the useful life has been changed due to plans to close certain facilities in the near term. Reversals of previously recorded layoff and other costs were primarily due to Alcoa's decision to sell certain locations that it previously planned to shut down in 2005.

While restructuring charges are not reflected in the segment results, the following table details what the impact of allocating these items to segment results would have been:

	2005	2004	2003
Alumina	$ 6	$(48)	$ (1)
Primary Metals	36	(1)	4
Flat-Rolled Products	15	1	13
Extruded and End Products	70	9	7
Engineered Solutions	109	8	(11)
Packaging and Consumer	39	10	(44)
Segment total	275	(21)	(32)
Corporate	17	(1)	5
Total restructuring and other charges	$292	$(22)	$(27)

The following discussion details the significant components of the 2005 restructuring program:

– In December 2005, the company temporarily curtailed production at its Eastalco, MD smelter because it was not able to secure a new, competitive power supply for the facility. A charge of $14 was recorded for the termination of approximately 550 people.

– The automotive operations, included in the Engineered Solutions segment, were restructured to improve efficiencies and included the following actions:

- A restructuring of the cast auto wheels business occurred, which ultimately included the sale of the wheels facility in Italy. Total charges recorded in 2005 were $71, consisting of $15 for severance costs associated with approximately 450 employees, $46 for asset impairments, and $10 loss on sale of the facility in Italy.

- Headcount reductions in the AFL automotive business resulted in a charge of $27 for the termination of approximately 3,900 employees, primarily in Mexico.

– The global extruded and end products businesses were restructured to optimize operations and increase productivity and included the following actions:

- Headcount reductions across various businesses resulted in a charge of $50 for the termination of 1,050 employees in the U.S., Europe, and Latin America.
- Charges of $15 were recorded for asset disposals at various U.S. and European extrusion plants related to certain assets which the businesses have ceased to operate.

– The restructuring associated with the packaging and consumer businesses consisted of plant consolidations and closures designed to strengthen the operations, resulting in charges of $39, comprised of $23 for the termination of 1,620 employees primarily in the U.S., $8 for asset disposals, and $8 for other exit costs. Other exit costs primarily consisted of accelerated depreciation.

Employee termination and severance costs were recorded based on approved detailed action plans submitted by the operating locations that specified positions to be eliminated, benefits to be paid under existing severance plans, union contracts or statutory requirements, and the expected timetable for completion of the plans. These terminations are expected to be completed in the next twelve months. As of December 31, 2005, 3,550 of the approximately 8,450 employees had been terminated. Approximately $69 of cash payments were made against the 2005 program reserves in 2005.

2004 Restructuring Program. During 2004, Alcoa recorded income of $22 ($41 after tax and minority interests) for restructuring and other items. The income recognized was comprised of the following components: a gain of $53 ($61 after tax and minority interests) on the sale of Alcoa’s specialty chemicals business and $15 resulting from adjustments to prior year reserves, offset by charges of $40 related to additional layoff reserves associated with approximately 4,100 hourly and salaried employees (located primarily in Mexico and the U.S.), as the company continued to focus on reducing costs, and $6 of asset impairments. The 2004 restructuring program is essentially complete. Approximately $16 of cash payments were made in 2005 related to prior year restructuring programs.

2003 Restructuring Program. During 2003, Alcoa recorded income of $27 ($25 after tax and minority interests) for restructuring and other charges. The income recognized was comprised of the following components: $44 of charges for employee termination and severance costs associated with approximately 1,600 hourly and salaried employees (located primarily in Europe, the U.S., and Brazil), as the company continued to focus on cost reductions in businesses that continued to be impacted by market declines; $33 of net favorable adjustments on assets held for sale; and $38 of income resulting from adjustments to prior year layoff reserves due to changes in facts and circumstances that led to changes in estimated costs. The 2003 restructuring program is essentially complete.

Activity and reserve balances for restructuring charges are as follows:

	Employee termination and severance costs	Other exit costs	Total
Reserve balances at December 31, 2002	$ 161	$ 84	$ 245
2003:			
Cash payments	(120)	(27)	(147)
2003 restructuring charges	44	—	44
Reversals of previously recorded restructuring charges	(38)	(9)	(47)
Reserve balances at December 31, 2003	$ 47	$ 48	$ 95
2004:			
Cash payments	(52)	(5)	(57)
2004 restructuring charges	40	—	40
Reversals of previously recorded restructuring charges	(11)	(4)	(15)
Reserve balances at December 31, 2004	$ 24	$ 39	$ 63
2005:			
Cash payments	(78)	(7)	(85)
2005 restructuring charges	238	6	244
Reversals of previously recorded restructuring charges	(48)	—	(48)
Reserve balances at December 31, 2005	$ 136	$ 38	$ 174

E. Goodwill and Other Intangible Assets

The following table details the changes in the carrying amount of goodwill.

December 31	2005	2004
Balance at beginning of year	$6,375	$6,277
Divestiture of businesses	(16)	—
Translation and other adjustments	(147)	98
Balance at end of year	$6,212	$6,375

The divestiture of businesses is primarily related to the sale of railroad assets within the Primary Metals segment.

The following tables detail other intangible assets.

December 31, 2005	Gross carrying amount	Accumulated amortization
Computer software	$ 763	$ (255)
Patents and licenses	154	(71)
Other intangibles	367	(117)
Total amortizable intangible assets	1,284	(443)
Indefinite-lived trade names and trademarks	166	—
Total other intangible assets	$1,450	$ (443)

December 31, 2004	Gross carrying amount	Accumulated amortization
Computer software	$ 685	$ (213)
Patents and licenses	154	(70)
Other intangibles	373	(118)
Total amortizable intangible assets	1,212	(401)
Indefinite-lived trade names and trademarks	173	—
Total other intangible assets	$1,385	$ (401)

Computer software costs consisted primarily of software costs associated with an enterprise business solution (EBS) within Alcoa to drive common systems among all businesses. Other intangibles, recorded within other assets in the Consolidated Balance Sheet, consisted primarily of customer relationship intangibles.

Amortization expense for intangible assets for the years ended December 31, 2005, 2004, and 2003 was $83, $73, and $76, respectively. Amortization expense is expected to be in the range of approximately $60 to $90 annually from 2006 to 2010.

F. Acquisitions and Divestitures

2005 Acquisitions. In December 2005, Alcoa purchased the remaining 30 percent minority interest in the Alcoa Closure Systems International (Tianjin) Co., Ltd. joint venture owned by its partner, China Suntrust Investment Group Co., Ltd., for $7 in cash. The joint venture, established in 1994 to produce plastic closures for beverages, is now a wholly-owned subsidiary.

In October 2005, Alcoa completed the formation of Alcoa Bohai Aluminum Industries Company Limited, a consolidated joint venture between Alcoa and the China International Trust & Investment (CITIC). Alcoa holds a 73% interest and will be the managing partner in the new venture, which will produce aluminum rolled products at the Bohai plant in Qinghuangdao, China. Alcoa is required to contribute an additional $115 in 2006 and $27 in 2007 to the new entity. The transaction resulted in $2 of goodwill.

In June 2005, Alcoa completed the purchase of the remaining 40 percent interest in the Alcoa (Shanghai) Aluminum Products Ltd. joint venture from its partner Shanghai Light Industrial Equipment (Group) Company, Ltd. for $16 in cash. Alcoa (Shanghai) Aluminum Products Ltd. is now a wholly-owned subsidiary and will continue to sell foil products to customers throughout Asia. The transaction resulted in $2 of goodwill.

On March 31, 2005, Alcoa finalized an agreement with Fujikura Ltd. of Japan in which Alcoa obtained complete ownership of the AFL automotive business and Fujikura obtained complete ownership of the AFL telecommunications business through a tax-free exchange. Fujikura exchanged all of its AFL shares for shares of a new telecommunications entity and $176 in cash. The transaction resulted in a reduction of goodwill for the AFL automotive business of $44, subject to adjustment based upon valuation and other studies that have not been completed. The agreement provides for a contingent payment to Fujikura in 2008 based upon the amount, if any, by which the average annual earnings from 2005 through 2007 for the automotive business exceed a targeted amount. This contingent payment, if paid, will be recorded as an adjustment to the transaction value. AFL automotive business results are recorded in the Engineered Solutions segment.

On January 31, 2005, Alcoa acquired two fabricating facilities located in the Russian Federation. The facilities, located in Belaya Kalitva and Samara, were purchased for $257 in cash. In connection with this transaction, Alcoa also made a $93 payment related to a long-term aluminum supply contract, which is recorded in other noncurrent assets in the accompanying financial statements. Based on the current purchase price allocation, no goodwill was recorded on this transaction. The final allocation of the purchase price will be based upon valuation and other studies, including environmental and other contingent liabilities, which will be completed in the first quarter of 2006. The purchase agreement also provides for contingent payments over the next five years based on the performance of the Russian facilities, with a potential carryforward period of an additional five years. The maximum amount of total contingent payments is $85. These contingent payments, if paid, will be recorded as an adjustment to purchase price. No contingent payments were made during 2005. The results of these facilities are recorded in the Flat-Rolled Products segment, the Extruded and End Products segment, and the Engineered Solutions segment.

2005 Divestitures. In December 2005, Alcoa completed the sale of its imaging and graphics communications business, Southern Graphic Systems, Inc. (SGS), to Citigroup Venture Capital Equity Partners, LP for $408 in cash and recognized a gain of $63 ($9 after tax). SGS was reflected in discontinued operations in the accompanying financial statements.

In September 2005, Alcoa sold its railroad assets to RailAmerica Transportation Corp., a subsidiary of RailAmerica Inc., for $78 in cash, resulting in a gain of $67 ($37 after tax). Alcoa and RailAmerica have entered into long-term service agreements under which RailAmerica will provide services to Alcoa facilities that utilize the railroads.

In September 2005, Alcoa completed the sale of its protective packaging business to Forest Resources LLC for $13 in cash and recorded a loss of $6 ($4 after tax). This business was reflected in discontinued operations in the accompanying financial statements.

In April 2005, Alcoa sold its stock in Elkem ASA (Elkem) to Orkla ASA for $869 in cash, resulting in a gain of $345 ($180 after tax), which was recorded in other income in the Statement of Consolidated Income.

In January 2005, Alcoa sold its interest in Integris Metals Inc., a metals distribution joint venture in which Alcoa owned a 50% interest, to Ryerson Tull. The investment was sold for $410 in cash and the assumption of Integris' debt, which was approximately $234. Alcoa received cash of $205, and no material gain or loss was recorded on the transaction.

2004 Acquisitions. During 2004, Alcoa completed two acquisitions at a cash cost of $2. None of these transactions had a material impact on Alcoa's financial statements.

2004 Divestitures. In 2004, Alcoa substantially completed its 2002 plan to divest certain noncore businesses, as outlined below:

During the fourth quarter of 2004, Alcoa sold an extrusion facility in Brazil, and no material gain or loss was recorded on the transaction. Alcoa also sold 40% of its interest in the Juruti bauxite project in Brazil to Alumina Limited, its partner in Alcoa World Alumina and Chemicals (AWAC). Alcoa holds 60% of AWAC, and Alumina Limited holds the remaining 40%. In exchange for 40% of Alcoa's interest in the Juruti

project, Alumina Limited contributed $40 to AWAC, and Alcoa realized a gain of $37 ($37 after tax) on the transaction.

During the second quarter of 2004, Alcoa sold its Russellville, AR and St. Louis, MO foil facilities and an extrusion facility in Europe for $37 in cash. Alcoa also sold its flexible packaging business in South America, which had been included in discontinued operations. There was no material gain or loss recognized on these transactions.

In the first quarter of 2004, Alcoa completed the sale of its specialty chemicals business to two private equity firms led by Rhone Capital LLC for an enterprise value of $342, which included the assumption of debt and other obligations. Alcoa received cash of $248 and recognized a gain of approximately $53 ($61 after tax and minority interests) in restructuring and other charges in the Statement of Consolidated Income.

Additionally, in the first quarter of 2004, Alcoa sold two businesses that were included in discontinued operations: the packaging equipment business was sold for $44 in cash and resulted in the recognition of a gain of $15 ($10 after tax), and the automotive fasteners business was sold for $17 in cash and notes receivable and resulted in an additional loss of $7 ($5 after tax).

2003 Acquisitions. In October 2003, Alcoa expanded its aluminum alliance with Kobe Steel Ltd. (Kobe) in Japan on the joint development of aluminum products for the automotive market. As part of this arrangement and due to changes in the business environment, Alcoa and Kobe discontinued their association in three can sheet joint ventures: KAAL Australia, KAAL Japan, and KAAL Asia. Based on terms of the agreement, Alcoa acquired from Kobe the remaining 50% interest in KAAL Australia, as well as the remaining 20% interest in KAAL Asia. In turn, Kobe purchased a 47% interest in KAAL Japan from Alcoa. These transactions, which were recorded at fair value, resulted in net cash proceeds to Alcoa of $9 and recognition of a gain of $17 ($26 after tax). Also, Alcoa and Kobe amended an existing aluminum supply agreement related to the KAAL Japan operations, which resulted in an acceleration of the delivery term of the agreement to two years.

In August of 2003, Alcoa acquired the remaining 40.9% shareholding in Alcoa Alumínio (Alumínio) held by Camargo Côrrea Group (Camargo Group) since 1984. Alcoa issued to the Camargo Group 17.8 million shares of Alcoa common stock, with a fair value of approximately $410, in exchange for the Camargo Group’s holdings. The agreement also provides for contingent payments through 2008, based on the performance of the South American operations. The maximum amount of contingent payments is $235. The contingent payments will be reduced by appreciation on the Alcoa shares issued in the transaction, as specified in the agreement. No contingent payments related to this agreement were required in 2004 or 2005. The purchase price allocation resulted in goodwill of approximately $56.

2003 Divestitures. In October of 2003, Alcoa completed the sale of its Latin America PET business to Amcor PET Packaging for $75, which resulted in an immaterial gain on the transaction. Alcoa also sold investments for approximately $129, comprised primarily of its interest in Latasa, a Latin America aluminum can business.

In connection with acquisitions made prior to 2003, Alcoa could be required to make additional payments of approximately $50 from 2006 through 2007 based upon the achievement of various financial and operating targets. During 2005, Alcoa made a contingent payment of approximately $13 related to the Fairchild acquisition, which was recorded as an adjustment to goodwill.

Pro forma results of the company, assuming all acquisitions had been made at the beginning of each period presented, would not have been materially different from the results reported.

G. Inventories

December 31	2005	2004
Finished goods	$ 962	$ 896
Work in process	1,024	899
Bauxite and alumina	486	456
Purchased raw materials	691	464
Operating supplies	229	214
	$3,392	$2,929

Approximately 44% of total inventories at December 31, 2005 were valued on a LIFO basis. If valued on an average-cost basis, total inventories would have been $858 and $680 higher at the end of 2005 and 2004, respectively.

H. Properties, Plants, and Equipment, at Cost

December 31	2005	2004
Land and land rights, including mines	$ 457	$ 460
Structures	6,255	6,116
Machinery and equipment	17,996	17,748
	24,708	24,324
Less: accumulated depreciation and depletion	13,661	13,086
	11,047	11,238
Construction work in progress	2,061	984
	$13,108	$12,222

I. Investments

December 31	2005	2004
Equity investments	$ 631	$1,517
Other investments	739	549
	$1,370	$2,066

Equity investments are primarily comprised of a 50% investment in Elkem Aluminium ANS, a joint venture between Alcoa and Elkem that owns and operates two aluminum smelters in Norway, and investments in several hydroelectric power construction projects in Brazil. See Note N for additional information. In 2005, Alcoa sold its 46.5% investment in Elkem and its 50% interest in Integris Metals Inc. During 2005, Alcoa recorded an impairment charge of $90 related to the closure of the Hamburger Aluminium-Werk facility, which was recorded in equity income.

Other investments are primarily comprised of Alcoa’s 8% interest in Aluminum Corporation of China (Chalco). The investment in Chalco is classified as an available-for-sale security and is carried at fair value, with unrealized gains/losses recorded in other comprehensive income. Cumulative unrealized gains, net of taxes, were $318 in 2005 and $221 in 2004.

J. Other Assets

December 31	2005	2004
Intangibles, net (E)	$1,007	$ 984
Deferred income taxes	1,600	1,604
Prepaid pension benefit (W)	144	83
Deferred charges and other	1,333	1,148
	$4,084	$3,819

K. Debt

Long-Term Debt.

December 31	2005	2004
4.25% Notes, due 2007	$ 792	$ 800
6.625% Notes, due 2008	150	150
7.375% Notes, due 2010	1,000	1,000
6.5% Notes, due 2011	1,000	1,000
6% Notes, due 2012	1,000	1,000
5.375% Notes, due 2013	600	600
6.5% Bonds, due 2018	250	250
6.75% Bonds, due 2028	300	300
Medium-term notes, due 2006–2013 (8.1% and 8.2% average rates)	110	142
Alcoa Alumínio		
7.5% Export notes, due 2006–2008	58	74
Fair value adjustments	(37)	33
Other	114	53
	5,337	5,402
Less: amount due within one year	58	57
	$5,279	$5,345

The amount of long-term debt maturing in each of the next five years, including the effects of fair value adjustments, is $58 in 2006, $857 in 2007, $281 in 2008, $32 in 2009, and $1,007 in 2010.

Alcoa Alumínio's export notes are collateralized by receivables due under an export contract. Certain financial ratios must be maintained, including the maintenance of a minimum debt service ratio, as well as a certain level of tangible net worth of Alumínio and its subsidiaries. The tangible net worth calculation excludes the effects of foreign currency changes.

The fair value adjustments result from changes in the carrying amounts of certain fixed-rate borrowings that have been designated as being hedged. Of the $(37) in 2005, $(100) related to outstanding hedges and $63 related to hedges that were settled early. Of the $33 in 2004, $(42) related to outstanding hedges and $75 related to hedges that were settled early. The adjustments for hedges that were settled early are being recognized as reductions of interest expense over the remaining maturity of the related debt (through 2028). For additional information on interest rate swaps, see Note X.

In 2004, Alcoa retired early $1,200 of debt securities, consisting of the following: $200 of 6.125% Bonds due in 2005, $500 of 7.25% Notes due in 2005, and $500 of 5.875% Notes due in 2006. These debt securities were retired primarily with proceeds from commercial paper borrowings and cash provided from operations. Alcoa recognized a net gain of $58 in other income on the early retirement of long-term debt and the associated settlement of interest rate swaps. The net gain of $58 is comprised of the following:

- a premium paid for early retirement of debt and related expenses of $67;
- a gain of $48 from previously settled interest rate swaps that hedged the retired debt and was reflected as an increase in its carrying value; and
- a gain of $77 from the settlement of interest rate swaps that hedged anticipated borrowings between June 2005 and June 2006. See Note X for additional information.

Commercial Paper. Commercial paper was $912 at December 31, 2005 and $630 at December 31, 2004. Commercial paper matures at various times within one year and has an annual weighted average interest rate of 4.3%. Alcoa maintains $3,000 of revolving-credit agreements with varying expiration dates as backup to its commercial paper program. In April 2005, Alcoa refinanced its $1,000 revolving-credit agreement that was to expire in April 2005 into a new $1,000 revolving-credit agreement that will expire in April 2010. Alcoa also has a $1,000 revolving-credit agreement that will expire in April 2008 and a $1,000 revolving-credit agreement that will expire in April 2009. Under these agreements, a certain ratio of indebtedness to consolidated net worth must be maintained. There were no amounts outstanding under the revolving-credit agreements at December 31, 2005. The interest rate on the agreements expiring in 2008 and 2009, if drawn upon, is Libor plus 17 basis points, which is subject to adjustment if Alcoa's credit rating changes, to a maximum interest rate of Libor plus 83.5 basis points. The interest rate on the agreement expiring in 2010, if drawn upon, is Libor plus 18 basis points, which is subject to adjustment if Alcoa's credit rating changes, to a maximum interest rate of Libor plus 60 basis points.

Short-Term Borrowings. Short-term borrowings included $233 and $216 at December 31, 2005 and 2004, respectively, related to accounts payable settlement arrangements with certain vendors and third-party intermediaries.

L. Other Noncurrent Liabilities and Deferred Credits

December 31	2005	2004
Deferred alumina sales revenue	$ 164	$ 179
Deferred aluminum sales revenue	186	260
Environmental remediation (Y)	350	318
Deferred credits	88	96
Asset retirement obligations	238	204
Other noncurrent liabilities	795	668
	$1,821	$1,725

M. Minority Interests

The following table summarizes the minority shareholders' interests in the equity of consolidated subsidiaries.

December 31	2005	2004
Alcoa of Australia	$ 888	$ 798
Alcoa World Alumina LLC	236	200
Alcoa Fujikura Ltd. (F)	—	273
Other	241	145
	$1,365	$1,416

N. Commitments and Contingencies

Various lawsuits, claims and proceedings have been or may be instituted or asserted against Alcoa, including those pertaining to environmental, product liability, and safety and health matters. While the amounts claimed may be substantial, the ultimate liability cannot now be determined because of the considerable uncertainties that exist. Therefore, it is possible that results of operations or liquidity in a particular period could be materially affected by certain contingencies. However, based on facts currently available, management believes that the disposition of matters that are pending or asserted will not have a materially adverse effect on the financial position or liquidity of the company.

Alcoa Alumínio S.A. (Alumínio), a wholly-owned subsidiary of Alcoa, is a participant in several hydroelectric power construction projects in Brazil for purposes of increasing its energy self-sufficiency and providing a long-term, low-cost source of power for its facilities.

The Machadinho project was completed in 2002. Alumínio committed to taking a share of the output of the completed Machadinho project for 30 years at cost (including cost of financing the project). In the event that other participants in this project fail to fulfill their financial responsibilities, Alumínio may be required to fund a portion of the deficiency. In accordance with the agreement, if Alumínio funds any such deficiency, its participation and share of the output from the project will increase proportionately.

The Barra Grande project was completed in November 2005 and is expected to reach full capacity in May 2006. Alumínio accounts for the Machadinho and Barra Grande hydroelectric projects on the equity method. Its total investment in these projects was $152 and $124 at December 31, 2005 and 2004, respectively. Alcoa's maximum exposure to loss on these completed projects is $447, which represents Alcoa's investment and guarantees of debt.

In October of 2004, Alcoa agreed to acquire a 20% interest in a consortium formed to acquire the Dampier to Bunbury Natural Gas Pipeline (DBNGP) in Western Australia in exchange for an initial cash investment of $17, which was classified as an equity investment. Alcoa has made additional contributions of $19 and committed to invest an additional $53 to be paid as the pipeline expands through 2008. The investment in the DBNGP was made in order to secure a competitively priced long-term supply of power to Alcoa's refineries in Western Australia. In addition to its equity ownership, Alcoa has an agreement to purchase gas transmission services from the DBNGP with the ability to terminate the agreement at its discretion. Alcoa's maximum exposure to loss on the investment and the related contract is approximately $300.

Alcoa is party to unconditional purchase obligations that expire between 2006 and 2017. Commitments related to these contracts total $92 in 2006, $97 in 2007, $92 in 2008, $78 in 2009, $75 in 2010, and $306 thereafter. Expenditures under these contracts totaled $26 in 2005, $23 in 2004, and $21 in 2003. Additionally, Alcoa has entered into other purchase commitments for energy and raw materials which total $2,217 in 2006, $1,115 in 2007, $838 in 2008, $614 in 2009, $560 in 2010, and $6,192 thereafter.

Alcoa has standby letters of credit related to environmental, insurance, and other activities. The total amount committed under these letters of credit, which expire at various dates in 2006 through 2015, was $501 at December 31, 2005.

Alcoa has issued guarantees, primarily related to project financing for the Machadinho and Barra Grande hydroelectric power projects in Brazil. The total amount committed under these guarantees, which expire at various dates in 2006 through 2017, was $431 at December 31, 2005.

O. Other Income, Net

	2005	2004	2003
Equity income	$ 26	$145	$138
Interest income	65	41	38
Foreign currency losses	(27)	(30)	(83)
Net gains on sales of assets	406	44	37
Net gain on early retirement of debt and interest rate swap settlements (K)	—	58	—
Other income	10	12	143
	$480	$270	$273

Equity income in 2005 included an impairment charge of $90 related to the closure of the Hamburger Aluminium-Werk facility in Hamburg, Germany. The charge is comprised of $65 for asset impairments and $25 for employee layoff costs and other shutdown costs. Net gains on sales of assets in 2005 included the $345 gain on the sale of Alcoa's stake in Elkem ASA and the $67 gain on the sale of railroad assets. Net gains on sales of assets in 2004 were primarily the result of the sale of Alcoa's 40% interest in the Juruti bauxite project in Brazil, which resulted in a $37 gain. Net gains on sales of assets in 2003 were primarily associated with dispositions of office space and other smaller noncore business assets. In 2004, Alcoa recognized a gain of $58 on the early retirement of long-term debt and the associated settlement of interest rate swaps. Other income in 2003 included a $105 gain from insurance settlements of a series of historical environmental matters in the United States.

P. Cash Flow Information

Cash payments for interest and income taxes follow.

	2005	2004	2003
Interest	$386	$318	$352
Income taxes	413	294	303

The details related to acquisitions follow.

	2005	2004	2003
Fair value of assets acquired	$ 373	$ 7	$ 275
Liabilities assumed	(102)	(5)	(80)
Minority interests	190	—	224
Stock issued	—	—	(410)
Cash paid	461	2	9
Less: cash acquired	—	—	—
Net cash paid	$ 461	$ 2	$ 9

Q. Segment and Geographic Area Information

Alcoa is primarily a producer of aluminum products. Aluminum and alumina represent approximately three-fourths of Alcoa's revenues. Nonaluminum products include precision castings, industrial fasteners, consumer products, food

service and flexible packaging products, plastic closures, and electrical distribution systems for cars and trucks. Alcoa's segments are organized by product on a worldwide basis. Alcoa's management reporting system evaluates performance based on a number of factors; however, the primary measure of performance is the after-tax operating income (ATOI) of each segment. Certain items such as interest income, interest expense, foreign currency translation gains/losses, certain effects of LIFO inventory accounting, minority interests, restructuring and other charges, discontinued operations, and accounting changes are excluded from segment ATOI. In addition, certain expenses, such as corporate general administrative expenses and depreciation and amortization on corporate assets, are not included in segment ATOI. Segment assets exclude cash, cash equivalents, short-term investments, and all deferred taxes. Segment assets also exclude items such as corporate fixed assets, LIFO reserves, goodwill allocated to corporate, assets held for sale, and other amounts.

The accounting policies of the segments are the same as those described in the Summary of Significant Accounting Policies (Note A). Transactions among segments are established based on negotiation among the parties. Differences between segment totals and Alcoa's consolidated totals for line items not reconciled are primarily due to corporate allocations.

Alcoa's products are used worldwide in packaging, consumer products, transportation (including aerospace, automotive, truck trailer, rail, and shipping), building and construction, and industrial applications. Total exports from the U.S. from continuing operations were $2,021 in 2005, $1,825 in 2004, and $1,646 in 2003.

In January 2005, Alcoa realigned its organization structure, creating global groups to better serve customers and increase the ability to capture efficiencies. As a result, certain reportable segments have been reorganized to reflect the new organization. The businesses within the former Engineered Products segment and the Other "group" have been realigned to form the new Extruded and End Products segment and the new Engineered Solutions segment. Prior period amounts have been reclassified to reflect these changes. Additionally, the Alumina and Chemicals segment has been renamed the Alumina segment, to reflect the sale of the specialty chemicals business.

Alcoa's reportable segments are as follows.

Alumina. This segment consists of Alcoa's worldwide alumina system that includes the mining of bauxite, which is then refined into alumina. Alumina is sold directly to internal and external smelter customers worldwide or is processed into industrial chemical products. Alcoa's alumina operations in Australia are a significant component of this segment. Slightly more than half of Alcoa's alumina production is sold under supply contracts to third parties worldwide, while the remainder is used internally. In the first quarter of 2004, Alcoa sold its specialty chemicals business.

Primary Metals. This segment consists of Alcoa's worldwide smelter system. Primary Metals receives alumina primarily from the Alumina segment and produces aluminum ingot to be used by Alcoa's fabricating businesses, as well as sold to external customers, aluminum traders, and commodity markets. Results from the sale of aluminum powder, scrap, and excess power are also included in this segment, as well as the results from aluminum derivative contracts. Aluminum ingot produced by Alcoa and used internally is transferred to other segments at prevailing market prices. The sale of ingot represents approximately 90% of this segment's third-party sales.

Flat-Rolled Products. This segment's principal business is the production and sale of aluminum plate, sheet, and foil. This segment includes rigid container sheet (RCS), which is sold directly to customers in the packaging and consumer market and is used to produce aluminum beverage cans. Seasonal increases in RCS sales are generally experienced in the second and third quarters of the year. This segment also includes sheet and plate used in the transportation, building and construction, and distributor markets (mainly used in the production of machinery and equipment and consumer durables), of which approximately two-thirds is sold directly to customers, while the remainder is sold through distributors. Approximately two-thirds of the third-party sales in this segment are derived from sheet and plate, and foil used in industrial markets, while the remaining one-third of third-party sales consists of RCS. While the customer base for flat-rolled products is large, a significant amount of sales of RCS, sheet, and plate is to a relatively small number of customers.

Extruded and End Products. This segment consists of extruded products, some of which are further fabricated into a variety of end products, and includes hard- and soft-alloy extrusions and architectural extrusions. These products primarily serve the building and construction, distribution, aerospace, automotive, and commercial transportation markets. These products are sold directly to customers and through distributors.

Engineered Solutions. This segment includes titanium, aluminum, and super-alloy investment castings; forgings and fasteners; electrical distribution systems; aluminum wheels; and integrated aluminum structural systems used in the aerospace, automotive, commercial transportation, and power generation markets. These products are sold directly to customers and through distributors.

Packaging and Consumer. This segment includes consumer, foodservice, and flexible packaging products; food and beverage closures; and plastic sheet and film for the packaging industry. The principal products in this segment include aluminum foil; plastic wraps and bags; plastic beverage and food closures; flexible packaging products; thermoformed plastic containers; and extruded plastic sheet and film. Consumer products are marketed under brands including Reynolds Wrap®, Diamond®, Baco®, and Cut-Rite® wax paper. Seasonal increases generally occur in the second and fourth quarters of the year for such products as consumer foil and plastic wraps and bags, while seasonal slowdowns for closures generally occur in the fourth quarter of the year. Products are generally sold directly to customers, consisting of supermarkets, beverage companies, food processors, retail chains, and commercial foodservice distributors.

Alcoa's reportable segments, as reclassified for discontinued operations and assets held for sale, follow.

Segment information	Alumina	Primary Metals	Flat-Rolled Products	Extruded and End Products	Engineered Solutions	Packaging and Consumer	Total
2005							
Sales:							
Third-party sales	$2,130	$4,698	$ 6,836	$3,729	$ 5,032	$ 3,139	$ 25,564
Intersegment sales	1,707	4,808	128	64	—	—	6,707
Total sales	$3,837	$9,506	$ 6,964	$3,793	$ 5,032	$ 3,139	$ 32,271
Profit and loss:							
Equity income (loss)	$ —	$ (12)	$ —	$ —	$ 1	$ 1	$ (10)
Depreciation, depletion, and amortization	172	368	217	119	176	133	1,185
Income taxes	246	307	111	20	89	50	823
ATOI	682	822	288	39	203	105	2,139
Assets:							
Capital expenditures	$ 608	$ 869	$ 185	$ 114	$ 131	$ 100	$ 2,007
Equity investments	215	384	4	—	8	3	614
Goodwill	15	923	158	202	2,503	814	4,615
Total assets	4,268	8,566	3,963	2,021	5,733	2,787	27,338
2004							
Sales:							
Third-party sales	$1,975	$3,806	$ 5,962	$3,387	$ 4,563	$ 2,923	$ 22,616
Intersegment sales	1,418	4,335	89	54	—	—	5,896
Total sales	$3,393	$8,141	$ 6,051	$3,441	$ 4,563	$ 2,923	$ 28,512
Profit and loss:							
Equity income (loss)	$ 1	$ 58	$ (1)	$ —	$ —	$ 1	$ 59
Depreciation, depletion, and amortization	153	326	198	113	188	126	1,104
Income taxes	240	314	75	22	96	72	819
ATOI	632	808	246	62	216	141	2,105
Assets:							
Capital expenditures	$ 339	$ 281	$ 153	$ 99	$ 103	$ 73	$ 1,048
Equity investments	187	563	6	—	6	2	764
Goodwill	15	931	168	211	2,603	834	4,762
Total assets	3,605	8,121	3,672	1,935	5,701	2,805	25,839
2003							
Sales:							
Third-party sales	$2,002	$3,229	$ 4,815	$3,003	$ 4,325	$ 2,894	$ 20,268
Intersegment sales	1,021	3,098	66	34	—	—	4,219
Total sales	$3,023	$6,327	$ 4,881	$3,037	$ 4,325	$ 2,894	$ 24,487
Profit and loss:							
Equity income (loss)	$ —	$ 55	$ (1)	$ —	$ —	$ 3	$ 57
Depreciation, depletion, and amortization	147	310	192	104	191	126	1,070
Income taxes	161	256	70	3	100	85	675
ATOI	415	657	221	33	190	188	1,704
Assets:							
Capital expenditures	$ 173	$ 169	$ 149	$ 81	$ 78	$ 76	$ 726
Equity investments	163	489	13	—	6	2	673
Goodwill	17	918	165	215	2,552	822	4,689
Total assets	3,077	7,398	3,380	1,948	5,924	2,787	24,514

The difference between the segment totals and consolidated totals is in Corporate.

The following reconciles segment information to consolidated totals.

	2005	2004	2003
Sales:			
Total sales	$32,271	$28,512	$24,487
Elimination of intersegment sales	(6,707)	(5,896)	(4,219)
Corporate	4	(7)	14
Consolidated sales	$25,568	$22,609	$20,282
Net income:			
ATOI	$ 2,139	$ 2,105	$ 1,704
Impact of intersegment profit adjustments	37	52	9
Unallocated amounts (net of tax):			
Interest income	42	26	24
Interest expense	(220)	(176)	(204)
Minority interests	(259)	(245)	(238)
Corporate expense	(312)	(283)	(287)
Restructuring and other charges	(197)	23	26
Discontinued operations	(22)	(59)	(27)
Accounting changes	(2)	—	(47)
Other	27	(133)	(22)
Consolidated net income	$ 1,233	$ 1,310	$ 938
Assets:			
Total segment assets	$27,338	$25,839	$24,514
Elimination of intersegment receivables	(193)	(438)	(358)
Unallocated amounts:			
Cash, cash equivalents, and short-term investments	769	463	606
Deferred tax assets	1,797	1,884	1,610
Corporate goodwill	1,597	1,613	1,588
Corporate fixed assets	753	595	810
LIFO reserve	(858)	(680)	(543)
Assets held for sale	248	767	1,385
Other	2,245	2,566	2,099
Consolidated assets	$33,696	$32,609	$31,711

Geographic information for revenues and long-lived assets follows.

	2005	2004	2003
Revenues:			
U.S.	$14,923	$13,660	$12,050
Australia	2,464	1,971	1,615
Spain	1,451	1,307	1,119
United Kingdom	887	830	714
Hungary	855	604	493
Brazil	787	603	617
Germany	779	770	785
Other	3,418	2,871	2,875
	$25,564	$22,616	$20,268
Long-lived assets:*			
U.S.	$11,306	$11,691	$12,084
Canada	2,508	2,537	2,604
Australia	2,703	2,262	2,050
United Kingdom	750	869	828
Brazil	1,116	797	708
Iceland	505	108	15
Other	2,659	2,528	2,311
	$21,547	$20,792	$20,600

*Long-lived assets include intangible assets.

R. Preferred and Common Stock

Preferred Stock. Alcoa has two classes of preferred stock. Serial preferred stock has 660,000 shares authorized and 546,024 shares outstanding, with a par value of $100 per share and an annual $3.75 cumulative dividend preference per share. Class B serial preferred stock has 10 million shares authorized (none issued) and a par value of $1 per share.

Common Stock. There are 1.8 billion shares authorized at a par value of $1 per share. As of December 31, 2005, 133 million shares of common stock were reserved for issuance under the long-term stock incentive plans.

Stock options under the company's stock incentive plans have been granted, at not less than market prices on the dates of grant. Stock option features based on date of original grant are as follows:

Date of original grant	Vesting	Term	Reload feature
2002 and prior	One year	10 years	One reload over option term
2003	3 years (1/3 each year)	10 years	One reload in 2004 for 1/3 vesting in 2004
2004 and forward	3 years (1/3 each year)	6 years	None

The transactions for shares under options were: (shares in millions)

	2005	2004	2003
Outstanding, beginning of year:			
Number of options	89.6	87.8	81.6
Weighted average exercise price	$33.34	$32.50	$33.19
Granted:			
Number of options	7.0	8.8	16.8
Weighted average exercise price	$29.48	$35.63	$24.93
Exercised:			
Number of options	(3.7)	(5.6)	(8.0)
Weighted average exercise price	$20.14	$23.34	$23.29
Expired or forfeited:			
Number of options	(4.3)	(1.4)	(2.6)
Weighted average exercise price	$35.34	$37.87	$32.58
Outstanding, end of year:			
Number of options	88.6	89.6	87.8
Weighted average exercise price	$33.50	$33.34	$32.50
Exercisable, end of year:			
Number of options	84.4	73.5	71.6
Weighted average exercise price	$34.03	$34.39	$34.22
Shares available for future options	32.4	35.1	13.1

The following tables summarize certain stock option information at December 31, 2005: (shares in millions)

Options Outstanding

Range of exercise price	Number	Weighted average remaining life	Weighted average exercise price
$ 4.38 - $12.15	0.3	1.00	$ 11.46
$12.16 - $19.93	1.6	1.63	16.78
$19.94 - $27.71	13.8	5.54	22.58
$27.72 - $35.49	23.0	3.99	31.06
$35.50 - $45.59	49.9	3.89	38.30
Total	88.6	4.12	33.50

Options Exercisable

Range of exercise price	Number	Weighted average exercise price
$ 4.38 - $12.15	0.3	$ 11.46
$12.16 - $19.93	1.6	16.78
$19.94 - $27.71	9.7	22.58
$27.72 - $35.49	22.9	31.06
$35.50 - $45.59	49.9	38.30
Total	84.4	34.03

Beginning in January of 2004, in addition to stock option awards, the company has granted stock awards and performance share awards. Both vest three years from the date of grant. Performance share awards are issued at target and the final award amount is determined at the end of the performance period.

The following table summarizes the non-vested stock and performance share awards: (shares in millions)

	2005	2004
Outstanding, beginning of year	1.5	—
Granted	1.7	1.5
Forfeited	(0.2)	—
Performance share adjustment	(0.4)	—
Outstanding, end of year	2.6	1.5
Shares reserved for future grants	9.3	10.5
After-tax compensation expense	$ 16	$ 9

Share Activity (number of shares)

	Common stock	
	Treasury	Net outstanding
Balance at end of 2002	(79,755,076)	844,819,462
Stock issued:		
Alcoa Alumínio minority interest acquisition (F)	17,773,541	17,773,541
Compensation plans	5,897,683	5,897,683
Balance at end of 2003	(56,083,852)	868,490,686
Treasury shares purchased	(1,777,354)	(1,777,354)
Stock issued:		
Compensation plans	4,266,751	4,266,751
Balance at end of 2004	(53,594,455)	870,980,083
Treasury shares purchased	(4,334,000)	(4,334,000)
Stock issued:		
Compensation plans	3,622,430	3,622,430
Balance at end of 2005	(54,306,025)	870,268,513

There were 546,024 shares of preferred stock outstanding and 924,574,538 shares of common stock issued at the end of each year presented.

S. Earnings Per Share

Basic earnings per common share (EPS) amounts are computed by dividing earnings after the deduction of preferred stock dividends by the average number of common shares outstanding. Diluted EPS amounts assume the issuance of common stock for all potentially dilutive equivalents outstanding.

The information used to compute basic and diluted EPS on income from continuing operations follows. (shares in millions)

	2005	2004	2003
Income from continuing operations	$1,257	$1,369	$1,012
Less: preferred stock dividends	2	2	2
Income from continuing operations available to common shareholders	$1,255	$1,367	$1,010
Average shares outstanding—basic	871.7	869.9	853.4
Effect of dilutive securities:			
Shares issuable upon exercise of dilutive stock options	5.2	7.5	3.2
Average shares outstanding—diluted	876.9	877.4	856.6

Options to purchase 73 million shares of common stock at an average exercise price of $36 per share were outstanding as of December 31, 2005. Options to purchase 56 million shares of common stock at an average exercise price of $38 per share were outstanding as of December 31, 2004. Options to purchase 51 million shares of common stock at an average exercise price of $38 per share were outstanding as of December 31, 2003. These amounts were not included in the computation of diluted EPS because the option exercise price was greater than the average market price of the common shares.

T. Income Taxes

The components of income from continuing operations before taxes on income were:

	2005	2004	2003
U.S.	$ 220	$ 257	$ 310
Foreign	1,750	1,896	1,335
	$1,970	$2,153	$1,645

The provision for taxes on income from continuing operations consisted of:

	2005	2004	2003
Current:			
U.S. federal*	$ (50)	$ 174	$ (54)
Foreign	482	445	304
State and local	38	15	17
	470	634	267
Deferred:			
U.S. federal*	25	(161)	132
Foreign	(28)	54	(4)
State and local	(13)	12	—
	(16)	(95)	128
Total	$454	$ 539	$395

*Includes U.S. taxes related to foreign income

Included in discontinued operations is a tax cost of $57 in 2005 and tax benefits of $6 in 2004 and $17 in 2003.

The exercise of employee stock options generated a tax benefit of $9 in 2005, $21 in 2004, and $23 in 2003. This amount was credited to additional capital and reduced current taxes payable.

Reconciliation of the U.S. federal statutory rate to Alcoa's effective tax rate for continuing operations follows.

	2005	2004	2003
U.S. federal statutory rate	35.0%	35.0%	35.0%
Taxes on foreign income	(7.5)	(9.6)	(7.5)
State taxes net of federal benefit	0.8	0.7	0.9
Minority interests	0.6	0.5	1.1
Permanent differences on asset disposals	2.4	(1.1)	(0.1)
Audit and other adjustments to prior years' accruals*	(7.0)	0.7	(4.1)
Other	(1.3)	(1.2)	(1.3)
Effective tax rate	23.0%	25.0%	24.0%

*2005 includes the finalization of certain tax reviews and audits, decreasing the effective tax rate by approximately 6.2 percentage points.

The components of net deferred tax assets and liabilities follow.

	2005		2004	
December 31	Deferred tax assets	Deferred tax liabilities	Deferred tax assets	Deferred tax liabilities
Depreciation	$ —	$ 1,432	$ —	$ 1,434
Employee benefits	1,455	—	1,422	—
Loss provisions	392	—	420	—
Deferred income/expense	116	188	113	202
Tax loss carryforwards	492	—	498	—
Tax credit carryforwards	206	—	348	—
Unrealized gains on available-for-sale securities	—	171	—	119
Other	218	178	199	156
	2,879	1,969	3,000	1,911
Valuation allowance	(127)	—	(120)	—
	$ 2,752	$ 1,969	$ 2,880	$ 1,911

Of the total deferred tax assets associated with the tax loss carryforwards, $86 expires over the next ten years, $183 over the next 20 years, and $223 is unlimited. Of the tax credit carryforwards, $92 is unlimited, with the balance expiring over
the next ten years. A substantial portion of the valuation allowance relates to the loss carryforwards because the ability to generate sufficient foreign taxable income in future years is uncertain. The net change in the valuation allowance for foreign net operating losses and tax credits resulted in a tax cost of $7 in 2005 and the recognition of a tax benefit of $21 in 2004. Approximately $31 of the valuation allowance relates to acquired companies for which subsequently recognized benefits will reduce goodwill.

The cumulative amount of Alcoa's foreign undistributed net earnings for which no deferred taxes have been provided was $7,562 at December 31, 2005. Management has no plans to distribute such earnings in the foreseeable future. It is not practical to determine the deferred tax liability on these earnings. Alcoa did not utilize the American Job Creation Act of 2004 provision that allows companies to repatriate earnings from foreign subsidiaries at a reduced U.S. tax rate.

U. Lease Expense

Certain equipment, warehousing and office space, and ocean-going vessels are under operating lease agreements. Total expense from continuing operations for all leases was $261 in 2005, $245 in 2004, and $214 in 2003. Under long-term operating leases, minimum annual rentals are $214 in 2006, $176 in 2007, $131 in 2008, $109 in 2009, $118 in 2010, and a total of $273 for 2011 and thereafter.

V. Interest Cost Components

	2005	2004	2003
Amount charged to expense	$339	$271	$314
Amount capitalized	58	27	21
	$397	$298	$335

W. Pension Plans and Other Postretirement Benefits

Alcoa maintains pension plans covering most U.S. employees and certain other employees. Pension benefits generally depend on length of service, job grade, and remuneration. Substantially all benefits are paid through pension trusts that are sufficiently funded to ensure that all plans can pay benefits to retirees as they become due. Most U.S. salaried and non-union hourly employees hired after March 1, 2006 will participate in a defined contribution plan instead of the current defined benefit plan.

Alcoa maintains health care and life insurance benefit plans covering most eligible U.S. retired employees and certain other retirees. Generally, the medical plans pay a percentage of medical expenses, reduced by deductibles and other coverages. These plans are generally unfunded, except for certain benefits funded through a trust. Life benefits are generally provided by insurance contracts. Alcoa retains the right, subject to existing agreements, to change or eliminate these benefits. All U.S. salaried and certain hourly employees hired after January 1, 2002 will not have postretirement health care benefits. Alcoa uses a December 31 measurement date for the majority of its plans.

Obligations and Funded Status

December 31	Pension benefits		Postretirement benefits	
	2005	2004	2005	2004
Change in projected benefit obligation				
Benefit obligation at beginning of year	$10,751	$10,268	$ 3,829	$ 3,661
Service cost	209	204	33	31
Interest cost	619	617	216	221
Amendments	—	(4)	(26)	(6)
Actuarial losses (gains)	487	220	(47)	276
Acquisitions	20	—	—	—
Divestitures	(5)	(10)	(1)	—
Benefits paid, net of participants' contributions	(685)	(668)	(349)	(355)
Other transfers, net	—	46	—	—
Exchange rate	(64)	78	1	1
Projected benefit obligation at end of year	$11,332	$10,751	$ 3,656	$ 3,829
Change in plan assets				
Fair value of plan assets at beginning of year	$ 8,800	$ 8,386	$ 157	$ 137
Actual return on plan assets	866	927	13	20
Acquisitions	16	—	—	—
Employer contributions	383	101	—	—
Participants' contributions	26	24	—	—
Benefits paid	(690)	(676)	—	—
Administrative expenses	(24)	(28)	—	—
Other transfers, net	—	27	—	—
Exchange rate	(54)	39	—	—
Fair value of plan assets at end of year	$ 9,323	$ 8,800	$ 170	$ 157
Funded status	$ (2,009)	$ (1,951)	$ (3,486)	$ (3,672)
Unrecognized net actuarial loss	2,187	1,912	1,028	1,133
Unrecognized net prior service cost (benefit)	51	73	(37)	(7)
Net amount recognized	$ 229	$ 34	$ (2,495)	$ (2,546)
Amounts recognized in the Consolidated Balance Sheet consist of:				
Prepaid benefit	$ 150	$ 83	$ —	$ —
Accrued benefit liability	(1,674)	(1,587)	(2,495)	(2,546)
Intangible asset	35	53	—	—
Accumulated other comprehensive loss	1,718	1,485	—	—
Amount recognized	229	34	(2,495)	(2,546)
Amounts attributed to joint venture partners	10	17	38	38
Net amount recognized	$ 239	$ 51	$ (2,457)	$ (2,508)

Components of Net Periodic Benefit Costs

	Pension benefits			Postretirement benefits		
	2005	2004	2003	2005	2004	2003
Service cost	$ 209	$ 204	$ 194	$ 33	$ 31	$ 31
Interest cost	619	617	609	216	221	237
Expected return on plan assets	(719)	(719)	(727)	(14)	(13)	(11)
Amortization of prior service cost (benefit)	22	39	38	4	(6)	(32)
Recognized actuarial loss	95	61	8	59	46	40
Net periodic benefit costs	$ 226	$ 202	$ 122	$298	$279	$265

An increase in the minimum pension liability resulted in a charge to shareholders' equity of $148 in 2005 and $21 in 2004.

The projected benefit obligation for all defined benefit pension plans was $11,332 and $10,751 at December 31, 2005 and 2004, respectively.

The accumulated benefit obligation for all defined benefit pension plans was $10,876 and $10,326 at December 31, 2005 and 2004, respectively.

The aggregate projected benefit obligation and fair value of plan assets for the pension plans with benefit obligations in excess of plan assets were $11,071 and $8,982, respectively, as of December 31, 2005, and $10,518 and $8,343, respectively, as of December 31, 2004. The aggregate accumulated benefit obligation and fair value of plan assets with accumulated benefit obligations in excess of plan assets were $10,163 and $8,504, respectively, as of December 31, 2005, and $10,086 and $8,320, respectively, as of December 31, 2004.

At December 31, 2005 and 2004, the long-term accrued pension benefits on the Consolidated Balance Sheet were $1,500 and $1,513, respectively. The total accrued benefit liability was $1,674 in 2005 and $1,587 in 2004, which included the current portion of the liability of $154 in 2005 and $57 in 2004 and the amounts attributed to joint venture partners of $20 in 2005 and $17 in 2004. At December 31, 2005 and 2004, the prepaid pension benefits on the Consolidated Balance Sheet were $144 and $83, respectively. The total prepaid benefit was $150 in 2005 and $83 in 2004, which included amounts attributed to joint venture partners of $6 in 2005. At December 31, 2005 and 2004, the intangible pension asset on the Consolidated Balance Sheet was $31 and $53, respectively. The total intangible asset was $35 in 2005 and $53 in 2004, which included amounts attributed to joint venture partners of $4 in 2005.

The unrecognized net actuarial loss for pension benefit plans at December 31, 2005 of $2,187 has primarily resulted from the decline in interest rates over the past four years. To the extent those losses exceed certain thresholds, the excess will continue to be recognized as prescribed under SFAS No. 87, "Employers' Accounting for Pensions." Generally, these amounts are amortized over the estimated future service of plan participants, which is 14 years.

The benefit obligation for postretirement benefit plans and net amount recognized were $3,656 and $2,495, respectively, as of December 31, 2005, and $3,829 and $2,546, respectively, as of December 31, 2004. Of the net amount recognized, the long-term, current, and amounts attributed to joint venture partners were $2,105, $352, and $38, respectively, as of December 31, 2005, and $2,150, $358, and $38, respectively, as of December 31, 2004.

On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) was signed into law. The Act introduced a prescription drug benefit under Medicare (Medicare Part D), as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D.

Currently, Alcoa pays a portion of the prescription drug cost for certain retirees. The benefits were determined to be actuarially equivalent based on an analysis of Alcoa's existing prescription drug plan provisions and claims experience as compared to the Medicare Part D prescription drug benefit that will be effective in 2006.

As of December 31, 2005 and 2004, Alcoa recognized the effects of the Act in the measure of its Accumulated Postretirement Benefit Obligation (APBO) for certain retiree groups in accordance with FASB Staff Position No. FAS 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." At December 31, 2003, recognition of the subsidy for certain retiree groups as an offset to plan costs resulted in a $190 reduction in the APBO. The reduction in the APBO is included with other deferred actuarial gains and losses. For other retiree groups not previously recognized at December 31, 2003, the impact of the potential subsidy benefit was recognized at December 31, 2005 and resulted in a $220 reduction to the APBO. Alcoa has not reflected any changes in participation in the company plan as a result of the Act. The reduction in APBO represents the value of the subsidy and does not reflect any other changes. The subsidy is estimated to reduce the prescription drug portion of the per capita cost by 24% for Medicare-eligible retirees.

The net periodic benefit cost for postretirement benefits for the year ended December 31, 2005 reflected a reduction of $24 related to the recognition of the federal subsidy under Medicare Part D. Subsequent net periodic postretirement benefit costs will be adjusted to reflect the lower interest cost due to the lower APBO. To the extent deferred gains and losses exceed certain thresholds, the excess will continue to be recognized as prescribed under SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." Additionally, the projected reduction to the 2006 net periodic postretirement benefit cost, due to the $220 reduction to the APBO determined in 2005, is $26.

The unrecognized net actuarial loss for postretirement benefit plans at December 31, 2005 of $1,028 primarily resulted from the decline in interest rates over the past four years. To the extent those losses exceed certain thresholds, the excess will continue to be recognized. Generally, these amounts are amortized over the estimated future service of plan participants, which is 12 years.

Assumptions

Weighted average assumptions used to determine benefit obligations are as follows:

December 31	2005	2004
Discount rate	5.70%	6.00%
Rate of compensation increase	4.00	4.50

The discount rate is determined using a yield curve model developed by the company's external actuaries. The plan's projected benefit obligation cash flows are discounted using yields on high quality corporate bonds to produce a single equivalent rate. The plan's cash flows have an average duration of 13 years.

The rate of compensation increase is based upon actual experience.

Weighted average assumptions used to determine the net periodic benefit cost are as follows:

	2005	2004	2003
Discount rate	6.00%	6.25%	6.75%
Expected long-term return on plan assets	9.00	9.00	9.00
Rate of compensation increase	4.50	5.00	5.00

The expected return on plan assets is based on historical performance as well as expected future rates of return on plan assets considering the current investment portfolio mix and the long-term investment strategy. The 10-year moving average of actual performance has consistently exceeded 9% over the past 20 years.

Assumed health care cost trend rates are as follows:

	2005	2004	2003
Health care cost trend rate assumed for next year	8.0%	8.0%	9.0%
Rate to which the cost trend rate gradually declines	5.0%	5.0%	5.0%
Year that the rate reaches the rate at which it is assumed to remain	2010	2009	2009

The health care cost trend rate in the calculation of the 2004 benefit obligation was 8.0% from 2004 to 2005 and 8.0% from 2005 to 2006. Actual annual company health care trend experience over the past three years has ranged from 5.0% to 7.5%. The 8% trend rate will be maintained for 2006.

Assumed health care cost trend rates have an effect on the amounts reported for the health care plan. A one-percentage point change in these assumed rates would have the following effects:

	1% increase	1% decrease
Effect on total of service and interest cost components	$ 8	$ (7)
Effect on postretirement benefit obligations	129	(108)

Plan Assets

Alcoa's pension and postretirement plans' investment policy, weighted average asset allocations at December 31, 2005 and 2004, and target allocations for 2006, by asset category, are as follows:

		Plan assets at December 31		Target %
Asset category	Policy range	2005	2004	2006
Equity securities	35–60%	57%	56%	53%
Debt securities	30–55%	34	35	35
Real estate	5–15%	5	5	6
Other	0–15%	4	4	6
Total		100%	100%	100%

The basic goal underlying the pension plan investment policy is to ensure that the assets of the plan, along with expected plan sponsor contributions, will be invested in a prudent manner to meet the obligations of the plan as those obligations come due. Investment practices must comply with the requirements of the Employee Retirement Income Security Act of 1974 (ERISA) and any other applicable laws and regulations.

Numerous asset classes with differing expected rates of return, return volatility, and correlations are utilized to reduce risk by providing diversification. Debt securities comprise a significant portion of the portfolio due to their plan-liability-matching characteristics and to address the plan's cash flow requirements. Additionally, diversification of investments within each asset class is utilized to further reduce the impact of losses in single investments. The use of derivative instruments is permitted where appropriate and necessary for achieving overall investment policy objectives.

Cash Flows

In 2005, contributions to Alcoa's pension plans were $383, of which $300 was voluntary. The minimum required cash contribution to the pension plans in 2006 is estimated to be $154.

Benefit payments expected to be paid to plan participants and expected subsidy receipts are as follows:

Year ended December 31	Pension benefits	Post-retirement benefits	Subsidy receipts
2006	$ 700	$ 352	$ 25
2007	700	350	25
2008	700	350	30
2009	750	350	30
2010	750	350	30
2011 through 2015	4,100	1,750	180
	$7,700	$ 3,502	$ 320

Other Plans

Alcoa also sponsors a number of defined contribution pension plans. Expenses were $127 in 2005, $118 in 2004, and $107 in 2003.

X. Other Financial Instruments and Derivatives

Other Financial Instruments. The carrying values and fair values of Alcoa's financial instruments follow.

	2005		2004	
December 31	Carrying value	Fair value	Carrying value	Fair value
Cash and cash equivalents	$ 762	$ 762	$ 457	$ 457
Short-term investments	7	7	6	6
Noncurrent receivables	138	138	18	18
Available-for-sale investments	733	733	527	527
Short-term debt	58	58	57	57
Short-term borrowings	300	300	267	267
Commercial paper	912	912	630	630
Long-term debt	5,279	5,576	5,345	5,967

The methods used to estimate the fair values of certain financial instruments follow.

Cash and Cash Equivalents, Short-Term Investments, Short-Term Debt, Short-Term Borrowings, and Commercial Paper. The carrying amounts approximate fair value because of the short maturity of the instruments.

Noncurrent Receivables. The fair value of noncurrent receivables is based on anticipated cash flows which approximates carrying value.

Available-for-Sale Investments. The fair value of investments is based on readily available market values. Investments in marketable equity securities are classified as "available for sale" and are carried at fair value.

Long-Term Debt. The fair value is based on interest rates that are currently available to Alcoa for issuance of debt with similar terms and remaining maturities.

Derivatives. Alcoa uses derivative financial instruments for purposes other than trading. Fair value gains (losses) of material hedging contracts were:

	2005	2004
Aluminum	$ 4	$211
Interest rates	(100)	(42)
Other commodities, principally natural gas	201	53
Currencies	83	38

Aluminum consists of hedge contracts with gains of $245. This is mostly offset by losses on embedded derivatives in power contracts in Iceland and Brazil and our share of losses on hedge contracts of Norwegian smelters that are accounted for under the equity method.

Fair Value Hedges

Aluminum. Customers often require Alcoa to enter into long-term, fixed-price commitments. These commitments expose Alcoa to the risk of higher aluminum prices between the time the order is committed and the time that the order is shipped. Alcoa's aluminum commodity risk management policy is to manage, principally through the use of futures and options contracts, the aluminum price risk associated with a portion of its firm commitments. These contracts cover known exposures, generally within three years.

Interest Rates. Alcoa uses interest rate swaps to help maintain a strategic balance between fixed- and floating-rate debt and to manage overall financing costs. As of December 31, 2005, the company had pay floating, receive fixed interest rate swaps that were designated as fair value hedges. These hedges effectively convert the interest rate from fixed to floating on $2,500 of debt, through 2018. For additional information on interest rate swaps and their effect on debt and interest expense, see Note K.

Currencies. Alcoa uses cross-currency interest rate swaps that effectively convert its U.S. dollar denominated debt into Brazilian reais debt at local interest rates.

There were no transactions that ceased to qualify as a fair value hedge in 2005.

Cash Flow Hedges

Interest Rates. There were no cash flow hedges of interest rate exposures outstanding as of December 31, 2005. Alcoa previously used interest rate swaps to establish fixed interest rates on anticipated borrowings between June 2005 and June 2006. Due to a change in forecasted borrowing requirements, resulting from the early retirement of debt in June 2004 and a forecasted increase in future operating cash flows resulting from improved market conditions, it was judged no longer probable that the anticipated borrowings would occur in 2005 and 2006. Therefore, Alcoa recognized $33 of gains that had been deferred on previously settled swaps and $44 of additional gains to terminate the remaining interest rate swaps. These gains were recorded in other income in the second quarter of 2004.

Currencies. Alcoa is subject to exposure from fluctuations in foreign currency exchange rates. Foreign currency exchange contracts may be used from time to time to hedge the variability in cash flows from the forecasted payment or receipt of currencies other than the functional currency. These contracts cover periods commensurate with known or expected exposures, generally within three years. The U.S. dollar notional amount of all foreign currency contracts was approximately $240 and $400 as of December 31, 2005 and 2004, respectively. The majority of these contracts were hedging foreign currency exposure in Brazil.

Commodities. Alcoa anticipates the continued requirement to purchase aluminum and other commodities such as natural gas, fuel oil, and electricity for its operations. Alcoa enters into futures and forward contracts to reduce volatility in the price of these commodities.

Other

Alcoa has also entered into certain derivatives to minimize its price risk related to other customer sales and pricing arrangements. Alcoa has not qualified these contracts for hedge accounting treatment and therefore, the fair value gains and losses on these contracts are recorded in earnings. The impact to earnings was not significant in 2005 and was a gain of $29 in 2004.

Alcoa has entered into power supply contracts that contain pricing provisions related to the LME aluminum price. The LME-linked pricing features are considered embedded derivatives. A majority of these embedded derivatives have been designated as cash flow hedges of future sales of aluminum. Gains and losses on the remainder of these embedded derivatives are recognized in earnings. The impact to earnings was a loss of $21 in 2005 and a loss of $24 in 2004.

The disclosures with respect to commodity prices, interest rates, and foreign exchange risk do not take into account the underlying commitments or anticipated transactions. If the underlying items were included in the analysis, the gains or losses on the futures contracts may be offset. Actual results will be determined by a number of factors that are not under Alcoa's control and could vary significantly from those factors disclosed.

Alcoa is exposed to credit loss in the event of nonperformance by counterparties on the above instruments, as well as credit or performance risk with respect to its hedged customers' commitments. Although nonperformance is possible, Alcoa does not anticipate nonperformance by any of these parties. Contracts are with creditworthy counterparties and are further supported by cash, treasury bills, or irrevocable letters of credit issued by carefully chosen banks. In addition, various master netting arrangements are in place with counterparties to facilitate settlement of gains and losses on these contracts.

For further information on Alcoa's hedging and derivatives activities, see Notes A and K.

Y. Environmental Matters

Alcoa continues to participate in environmental assessments and cleanups at a number of locations. These include approximately 35 owned or operating facilities and adjoining properties, approximately 33 previously owned facilities and adjoining properties, and approximately 61 waste sites, including Superfund sites. A liability is recorded for environmental remediation costs or damages when a cleanup program becomes probable and the costs or damages can be reasonably estimated. See Note A for additional information.

As assessments and cleanups proceed, the liability is adjusted based on progress made in determining the extent of remedial actions and related costs and damages. The liability can change substantially due to factors such as the nature and extent of contamination, changes in remedial requirements, and techno

logical changes. Therefore, it is not possible to determine the outcomes or to estimate with any degree of accuracy the potential costs for certain of these matters.

The following discussion provides additional details regarding the current status of Alcoa's significant sites where the final outcome cannot be determined or the potential costs in the future cannot be estimated.

Massena, NY—Alcoa has been conducting investigations and studies of the Grasse River, adjacent to Alcoa's Massena, NY plant site, under order from the U.S. Environmental Protection Agency (EPA) issued under the Comprehensive Environmental Response, Compensation and Liability Act, also known as Superfund. Sediments and fish in the river contain varying levels of polychlorinated biphenyl (PCB).

In 2002, Alcoa submitted an Analysis of Alternatives Report that detailed a variety of remedial alternatives with estimated costs ranging from $2 to $525. Because the selection of the $2 alternative (natural recovery) was considered remote, Alcoa adjusted the reserve for the Grasse River in 2002 to $30, representing the low end of the range of possible alternatives, as no single alternative could be identified as more probable than the others.

In June of 2003, based on river observations during the spring of 2003, the EPA requested that Alcoa gather additional field data to assess the potential for sediment erosion from winter river ice formation and breakup. The results of these additional studies, submitted in a report to the EPA in April of 2004, suggest that this phenomenon has the potential to occur approximately every 10 years and may impact sediments in certain portions of the river under all remedial scenarios. The EPA informed Alcoa that a final remedial decision for the river could not be made without substantially more information, including river pilot studies on the effects of ice formation and breakup on each of the remedial techniques. Alcoa submitted to EPA and EPA approved a Remedial Options Pilot Study (ROPS) to gather this information. The scope of this study includes sediment removal and capping, the installation of an ice control structure, and significant monitoring.

In May of 2004, Alcoa agreed to perform the study at an estimated cost of $35. Most of the construction work was completed in 2005 with monitoring proposed for 2006. The findings will be incorporated into a revised Analysis of Alternatives Report, which is expected to be submitted in 2007. This information will be used by the EPA to propose a remedy for the entire river.

Alcoa adjusted the reserves in the second quarter of 2004 to include the $35 for the ROPS. This was in addition to the $30 previously reserved. With the exception of the natural recovery remedy, none of the existing alternatives in the 2002 Analysis of Alternatives Report is more probable than the others, and the results of the ROPS are necessary to revise the scope and estimated cost of many of the current alternatives.

The EPA's ultimate selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA's Record of Decision is issued, which is expected in 2008 or later.

Sherwin, TX—In connection with the sale of the Sherwin alumina refinery in Texas, which was required to be divested as part of the Reynolds merger in 2000, Alcoa has agreed to retain responsibility for the remediation of then-existing environmental conditions, as well as a pro rata share of the final closure of the active waste disposal areas, which remain in use. Alcoa's share of the closure costs is proportional to the total period of operation of the active waste disposal areas. Alcoa estimated its liability for the active disposal areas by making certain assumptions about the period of operation, the amount of material placed in the area prior to closure, and the appropriate technology, engineering, and regulatory status applicable to final closure. The most probable cost for remediation has been reserved. It is reasonably possible that an additional liability, not expected to exceed $75, may be incurred if actual experience varies from the original assumptions used.

East St. Louis, IL—In response to questions regarding environmental conditions at the former East St. Louis, IL operations, Alcoa entered into an administrative order with the EPA in December 2002 to perform a remedial investigation and feasibility study of an area used for the disposal of bauxite residue from historic alumina refining operations. A draft feasibility study was submitted to the EPA in April 2005. The feasibility study includes remedial alternatives that range from no further action at $0 to significant grading, stabilization, and water management of the bauxite residue disposal areas at $75. Because the selection of the $0 alternative was considered remote, Alcoa increased the environmental reserve for this location by $15 in the second quarter of 2005, representing the low end of the range of possible alternatives which meets the remedy selection criteria, as no alternative could be identified as more probable than the others. The EPA has not completed a final review of the feasibility study, and the EPA's selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA's Record of Decision is issued.

Based on the foregoing, it is possible that Alcoa's results of operations, in a particular period, could be materially affected by matters relating to these sites. However, based on facts currently available, management believes that adequate reserves have been provided and that the disposition of these matters will not have a materially adverse effect on the financial position or liquidity of the company.

Alcoa's remediation reserve balance at the end of 2005 and 2004 was $390 and $391 (of which $40 and $73 were classified as a current liability), respectively, and reflects the most probable costs to remediate identified environmental conditions for which costs can be reasonably estimated. Remediation expenses charged to the reserve were approximately $53 in 2005, $46 in 2004, and $32 in 2003. These amounts include expenditures currently mandated, as well as those not required by any regulatory authority or third party. The reserve balance was increased by $52 in 2005, primarily due to the reserve recorded for the acquired Russian fabricating facilities in the first quarter and for the East St. Louis, IL facility which was recorded in the second quarter of 2005. In 2004, the reserve increased by $42, primarily for the additional reserve recorded for the Grasse River site.

Included in annual operating expenses are the recurring costs of managing hazardous substances and environmental programs. These costs are estimated to be about 2% of cost of goods sold.

Supplemental Financial Information (unaudited)

Quarterly Data

(dollars in millions, except per-share amounts)

The financial information for all periods presented has been reclassified to reflect assets held for sale and discontinued operations. See Note B to the Consolidated Financial Statements for further information.

	First	Second	Third	Fourth	Year
2005					
Sales	$6,099	$ 6,532	$6,401	$6,536	$25,568
Income from continuing operations	269	490	285	213	1,257
(Loss) income from discontinued operations (B)	(9)	(30)	4	13	(22)
Cumulative effect of accounting change (C)	—	—	—	(2)	(2)
Net income	260	460	289	224	1,233
Earnings (loss) per share:					
Basic:					
Income from continuing operations	.31	.56	.33	.24	1.44
(Loss) income from discontinued operations	(.01)	(.03)	—	.02	(.03)
Cumulative effect of accounting change	—	—	—	—	—
Net income	.30	.53	.33	.26	1.41
Diluted:					
Income from continuing operations	.31	.56	.32	.24	1.43
(Loss) income from discontinued operations	(.01)	(.04)	.01	.02	(.03)
Cumulative effect of accounting change	—	—	—	—	—
Net income	.30	.52	.33	.26	1.40

	First	Second	Third	Fourth	Year
2004					
Sales	$5,397	$ 5,737	$5,639	$5,836	$22,609
Income from continuing operations	346	392	284	347	1,369
Income (loss) from discontinued operations (B)	9	12	(1)	(79)	(59)
Net income	355	404	283	268	1,310
Earnings (loss) per share:					
Basic:					
Income from continuing operations	.40	.45	.33	.40	1.57
Income (loss) from discontinued operations	.01	.01	(.01)	(.09)	(.07)
Net income	.41	.46	.32	.31	1.50
Diluted:					
Income from continuing operations	.39	.45	.32	.39	1.56
Income (loss) from discontinued operations	.01	.01	—	(.09)	(.07)
Net income	.40	.46	.32	.30	1.49

Number of Employees

	2005	2004	2003
U.S.	45,300	47,800	49,300
Other Americas	35,800	35,200	35,300
Europe	39,300	28,500	27,700
Pacific	8,600	7,500	7,700
	129,000	119,000	120,000

EXHIBIT 99.2

SCHEDULE II – VALUATION AND QUALIFYING ACCOUNTS
FOR THE YEARS ENDED DECEMBER 31,
(in millions)

Col. A	Col. B	Col. C		Col. D	Col. E
		Additions			
Description	Balance at beginning of period	Charged to costs and expenses	Charged to other accounts	Deductions	Balance at end of period
Allowance for doubtful accounts:					
2005	$ 81	$ 12	$ (2)(A)	$ 16(B)	$ 75
2004	$ 96	$ 12	$ (0)(A)	$ 27(B)	$ 81
2003	$ 109	$ 9	$ 3(A)	$ 25(B)	$ 96
Income tax valuation allowance:					
2005	$ 120	$ (3)	$ 20(A)	$ 10(C)	$ 127
2004	$ 147	$ 0	$ (1)(A)	$ 26(C)	$ 120
2003	$ 171	$ 1	$ 15(A)	$ 40(C)	$ 147

Notes: (A) Collections on accounts previously written off, acquisition/divestiture of subsidiaries and foreign currency translation adjustments.
(B) Uncollectible accounts written off.
(C) Related primarily to utilization of tax loss carryforwards.

The financial information of all prior periods has been reclassified to reflect discontinued operations and assets held for sale.

EXHIBIT 99.3

COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES FOR THE YEAR ENDED DECEMBER 31
(in millions, except ratios)

	2005	2004	2003	2002	2001
Earnings:					
Income from continuing operations before taxes on income and before accounting change	$1,970	$2,153	$1,645	$ 948	$1,637
Minority interests' share of earnings of majority-owned subsidiaries without fixed charges	—	—	—	—	—
Less equity earnings	(26)	(145)	(138)	(72)	(118)
Fixed charges added to earnings	387	313	346	380	420
Distributed income of less than 50% owned persons	40	59	35	21	23
Amortization of capitalized interest:					
Consolidated	25	25	21	14	13
Proportionate share of 50% owned persons	—	—	—	—	—
Total earnings	$2,396	$2,405	$1,909	$1,291	$1,975
Fixed Charges:					
Interest expense:					
Consolidated	$ 339	$ 271	$ 314	$ 350	$ 371
Proportionate share of 50% owned persons	3	3	4	4	6
	342	274	318	354	377
Amount representative of the interest factor in rents:					
Consolidated	43	37	27	25	41
Proportionate share of 50% owned persons	2	2	1	1	2
	45	39	28	26	43
Fixed charges added to earnings	387	313	346	380	420
Interest capitalized:					
Consolidated	58	27	21	22	22
Proportionate share of 50% owned persons	—	—	—	—	—
	58	27	21	22	22
Total fixed charges	$ 445	$ 340	$ 367	$ 402	$ 442
Ratio of earnings to fixed charges	5.4	7.1	5.2	3.2	4.5

The financial information of all prior periods has been reclassified to reflect discontinued operations.

EXHIBIT 99.4

PART I – FINANCIAL INFORMATION
Item 1. – Financial Statements.

Alcoa and subsidiaries
Condensed Consolidated Balance Sheet (unaudited)
(in millions)

	March 31 2006	December 31 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 459	$ 762
Receivables from customers, less allowances of $77 in 2006 and $75 in 2005	3,304	2,860
Other receivables	411	427
Inventories (J)	3,734	3,392
Fair value of derivative contracts	465	520
Prepaid expenses and other current assets	889	713
Total current assets	9,262	8,674
Properties, plants, and equipment, at cost	27,331	26,769
Less: accumulated depreciation, depletion, and amortization	13,889	13,661
Net properties, plants, and equipment	13,442	13,108
Goodwill	6,225	6,212
Investments	1,644	1,370
Other assets	4,110	4,084
Assets held for sale (H)	246	248
Total assets	$34,929	$ 33,696
LIABILITIES		
Current liabilities:		
Short-term borrowings	$ 370	$ 300
Commercial paper	1,672	912
Accounts payable, trade	2,622	2,570
Accrued compensation and retirement costs	943	1,096
Taxes, including taxes on income	865	871
Other current liabilities	1,312	1,445
Long-term debt due within one year	59	58
Total current liabilities	7,843	7,252
Long-term debt, less amount due within one year	5,226	5,279
Accrued pension benefits	1,533	1,500
Accrued postretirement benefits	2,090	2,105
Other noncurrent liabilities and deferred credits	1,916	1,821
Deferred income taxes	907	875
Liabilities of operations held for sale (H)	94	126
Total liabilities	19,609	18,958
MINORITY INTERESTS	1,391	1,365
COMMITMENTS AND CONTINGENCIES (K)		
SHAREHOLDERS' EQUITY		
Preferred stock	55	55
Common stock	925	925
Additional capital	5,810	5,720
Retained earnings	9,818	9,345
Treasury stock, at cost	(1,933)	(1,899)
Accumulated other comprehensive loss (L)	(746)	(773)
Total shareholders' equity	13,929	13,373
Total liabilities and equity	$34,929	$ 33,696

The accompanying notes are an integral part of the consolidated financial statements.

Alcoa and subsidiaries
Condensed Statement of Consolidated Income (unaudited)
(in millions, except per-share amounts)

	First quarter ended March 31	
	2006	**2005**
Sales (M)	$ 7,111	$ 6,099
Cost of goods sold	5,344	4,828
Selling, general administrative, and other expenses	355	310
Research and development expenses	47	45
Provision for depreciation, depletion, and amortization	306	310
Restructuring and other charges (D)	1	45
Interest expense	92	78
Other income, net (F)	(35)	(36)
Total costs and expenses	6,110	5,580
Income from continuing operations before taxes on income	1,001	519
Provision for taxes on income (G)	282	190
Income from continuing operations before minority interests' share	719	329
Less: Minority interests' share	105	60
Income from continuing operations	614	269
Loss from discontinued operations (H)	(6)	(9)
NET INCOME	$ 608	$ 260
EARNINGS (LOSS) PER SHARE (I)		
Basic:		
Income from continuing operations	$ .71	$ .31
Loss from discontinued operations	(.01)	(.01)
Net income	$ .70	$ .30
Diluted:		
Income from continuing operations	$ .70	$ .31
Loss from discontinued operations	(.01)	(.01)
Net income	$ .69	$ .30
Dividends paid per common share	$ .15	$ .15

The accompanying notes are an integral part of the consolidated financial statements.

Alcoa and subsidiaries
Condensed Statement of Consolidated Cash Flows (unaudited)
(in millions)

	Three months ended March 31	
	2006	**2005**
CASH FROM OPERATIONS		
Net income	$ 608	$ 260
Adjustments to reconcile net income to cash from operations:		
Depreciation, depletion, and amortization	307	313
Deferred income taxes	(4)	36
Equity income, net of dividends	(9)	(11)
Restructuring and other charges (D)	1	45
Provision for doubtful accounts	3	4
Loss from discontinued operations (H)	6	9
Minority interests	105	60
Stock-based compensation (B)	28	5
Other	1	(13)
Changes in assets and liabilities, excluding effects of acquisitions and divestitures:		
Increase in receivables	(390)	(477)
Increase in inventories	(333)	(345)
Increase in prepaid expenses and other current assets	(86)	(53)
(Decrease) increase in accounts payable and accrued expenses	(271)	90
(Decrease) increase in taxes, including taxes on income	(43)	49
Cash paid on long-term aluminum supply contract	—	(93)
Pension contributions	(77)	(18)
Net change in noncurrent assets and liabilities	(27)	(54)
CASH USED FOR CONTINUING OPERATIONS	(181)	(193)
CASH USED FOR DISCONTINUED OPERATIONS	(32)	(46)
CASH USED FOR OPERATIONS	(213)	(239)
FINANCING ACTIVITIES		
Net changes to short-term borrowings	69	63
Common stock issued for stock compensation plans	46	23
Repurchase of common stock	(60)	—
Dividends paid to shareholders	(131)	(131)
Dividends paid to minority interests	(115)	(72)
Net change in commercial paper	760	1,002
Additions to long-term debt	6	45
Payments on long-term debt	(5)	(61)
CASH PROVIDED FROM FINANCING ACTIVITIES	570	869
INVESTING ACTIVITIES		
Capital expenditures	(591)	(344)
Capital expenditures of discontinued operations	(1)	(3)
Acquisition of minority interests	(1)	(176)
Acquisitions, net of cash acquired	—	(257)
Sale of investments	—	206
Change in short-term investments and restricted cash	(59)	(7)
Additions to investments	(33)	(5)
Other	18	2
CASH USED FOR INVESTING ACTIVITIES	(667)	(584)
EFFECT OF EXCHANGE RATE CHANGES ON CASH	7	(6)
Net change in cash and cash equivalents	(303)	40
Cash and cash equivalents at beginning of year	762	457
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 459	$ 497

The accompanying notes are an integral part of the consolidated financial statements.

A. Basis of Presentation - The Condensed Consolidated Financial Statements are unaudited. These statements include all adjustments, consisting of normal recurring adjustments, considered necessary by management to fairly state the results of operations, financial position, and cash flows. The results reported in these Condensed Consolidated Financial Statements are not necessarily indicative of the results that may be expected for the entire year. The year-end balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

This Form 10-Q report should be read in conjunction with Alcoa's Annual Report on Form 10-K for the year ended December 31, 2005, which includes all disclosures required by accounting principles generally accepted in the United States of America.

B. Stock-Based Compensation – On January 1, 2006, Alcoa adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), "Share-Based Payment," which requires the company to recognize compensation expense for stock-based compensation based on the grant date fair value. This expense must be recognized ratably over the requisite service period following the date of grant. Alcoa has elected the modified prospective application method for adoption, and prior periods financial statements have not been restated. Prior to January 1, 2006, Alcoa accounted for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations.

Stock options under Alcoa's stock-based compensation plans have been granted at not less than market prices on the dates of grant. Beginning in 2006, performance stock options were granted to certain individuals. The final number of options granted is based on the outcome of Alcoa's annual return on capital results against the results of a comparator group of companies. However, an individual can earn a minimum number of options if Alcoa's return on capital meets or exceeds its cost of capital. Stock option features based on date of original grant are as follows:

Date of original grant	Vesting	Term	Reload feature
2002 and prior	One year	10 years	One reload over option term
2003	3 years (1/3 each year)	10 years	One reload in 2004 for 1/3 vesting in 2004
2004 and forward	3 years (1/3 each year)	6 years	None

In addition to the stock options described above, Alcoa granted restricted stock units (stock awards) that vest in three years from the date of grant. Certain of these stock awards were granted with the same performance conditions described above for performance stock options.

The following table summarizes the total compensation expense recognized for all options and stock awards:

First quarter ended March 31	2006	2005
Compensation expense reported in income:		
Stock option grants	$ 3	$ —
Stock award grants	25	5
Total compensation expense before income taxes	28	5
Income tax benefit	8	2
Total compensation expense, net of income tax benefit	$20	$ 3

Prior to January 1, 2006, no stock-based compensation expense was recognized for stock options. As a result of the implementation of SFAS No. 123(R), Alcoa recognized additional compensation expense of $3 pre-tax. There were no stock-based compensation expenses capitalized in the first quarter of 2006 or 2005. Alcoa's net income and earnings per share for 2005 would have been reduced to the pro forma amounts shown below if compensation expense had been determined based on the fair value at the grant dates in accordance with SFAS No. 123, "Accounting for Stock-Based Compensation," and SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure an amendment of FASB Statement No. 123."

First quarter ended March 31	2005
Net income, as reported	$260
Add: compensation expense reported in net income, net of income tax	—
Less: compensation expense determined under the fair value method, net of income tax	9
Pro forma net income	$251
Basic earnings per share:	
As reported	$ .30
Pro forma	.29
Diluted earnings per share:	
As reported	$ .30
Pro forma	.29

As of January 1, 2005, Alcoa switched from the Black-Scholes pricing model to a lattice model to estimate fair value at grant date for future option grants. The fair value of each option is estimated on the date of grant or subsequent reload using the lattice pricing model with the following assumptions:

First quarter ended March 31	2006	2005
Weighted average fair value per option	$ 5.98	$ 6.18
Average risk-free interest rate	4.43-4.42%	2.65-4.20%
Expected dividend yield	2.0%	1.8%
Expected volatility	27-32%	27-35%
Expected annual forfeiture rate	3%	—
Expected exercise behavior	23%	32%
Expected life (years)	3.6	3.8

The range of risk-free interest rates is based on a yield curve of interest rates at the time of the grant based on the contractual life of the option. Expected dividend yield is based on a five-year average. Expected volatility is based on historical and implied volatilities over the term of the option. Alcoa utilizes historical option exercise and forfeiture data to estimate expected annual pre- and post-vesting forfeitures. The expected exercise behavior assumption represents a weighted average exercise ratio of gains resulting from historical employee exercise behavior. The 2006 expected exercise behavior assumption is based on exercise patterns for grants issued from 2000 forward.

The activity for stock options is as follows: (shares in millions)

	2006
Outstanding at January 1, 2006:	
Number of options	88.6
Weighted average exercise price	$ 33.50
Granted:	
Number of options	3.0
Weighted average exercise price	$ 28.95
Exercised:	
Number of options	(2.0)
Weighted average exercise price	$ 22.46
Expired or forfeited:	
Number of options	(3.3)
Weighted average exercise price	$ 36.87
Outstanding at March 31, 2006:	
Number of options	86.3
Weighted average exercise price	$ 33.46
Aggregate intrinsic value	$123.60
Exercisable at March 31, 2006:	
Number of options	83.2
Weighted average exercise price	$ 33.63
Aggregate intrinsic value	$119.70

The total intrinsic value of options exercised for the first quarter ended March 31, 2006, was $16. The cash received from exercises was $46 and the tax benefit realized was $5.

The following tables summarize certain stock option information at March 31, 2006: (shares in millions)

Options Fully Vested and/or Expected to Vest

Range of exercise price	Number	Weighted average contractual life	Weighted average exercise price	Intrinsic Value
$ 4.38 - $12.15	0.2	1.01	$ 11.43	$ 3.90
$12.16 - $19.93	1.3	1.60	17.11	17.30
$19.94 - $27.71	12.3	5.40	22.44	93.10
$27.72 - $35.49	25.1	4.05	30.78	9.30
$35.50 - $45.59	47.4	3.81	38.28	—
Total	86.3	4.07	33.46	$123.60

Options Fully Vested and Exercisable

Range of exercise price	Number	Weighted average contractual life	Weighted average exercise price	Intrinsic Value
$ 4.38 - $12.15	0.2	1.01	$ 11.43	$ 3.90
$12.16 - $19.93	1.3	1.60	17.11	17.30
$19.94 - $27.71	12.2	5.40	22.44	92.50
$27.72 - $35.49	22.1	3.81	31.03	6.00
$35.50 - $45.59	47.4	3.81	38.28	—
Total	83.2	4.00	33.63	$119.70

The following table summarizes the non-vested stock and performance options at March 31, 2006: (shares in millions)

Non-Vested Option Grants

	Number	Weighted average per option FMV
Non-vested at January 1, 2006	4.2	$ 5.51
Granted	3.0	5.98
Vested	(4.0)	5.48
Forfeited	(0.1)	5.55
Non-vested at March 31, 2006	3.1	5.99

The following table summarizes the non-vested stock and performance share awards at March 31, 2006: (shares in millions)

Non-Vested Awards

	Stock Awards	Performance Share Awards	Total	Weighted average FMV
Outstanding at January 1, 2006	2.1	0.5	2.6	$ 31.66
Granted	2.1	0.4	2.5	28.93
Forfeited	(0.1)	—	(0.1)	31.13
Performance share adjustment	—	(0.2)	(0.2)	29.54
Outstanding at March 31, 2006	4.1	0.7	4.8	30.37

As of March 31, 2006, there was $15 (pre-tax) and $83 (pre-tax) of unrecognized compensation expense related to non-vested stock option and stock award grants, respectively. This expense is expected to be recognized over a weighted average period of 2.1 years. As of March 31, 2006, the following table summarizes the unrecognized compensation expense expected to be recognized in future periods.

	Stock-based compensation expense (pre-tax)
Remainder of 2006	$ 41
2007	32
2008	25
Total	$ 98

Alcoa issues treasury shares for the exercise of employee stock options. As of March 31, 2006, 131 million shares of common stock were reserved for issuance under Alcoa's stock-based compensation plans. Alcoa has a policy of repurchasing shares to cover the dilution associated with option exercises and expects to repurchase shares in an amount that approximates options exercised during 2006.

C. Recently Adopted Accounting Standards – Effective January 1, 2006, Alcoa adopted Emerging Issues Task Force (EITF) Issue No. 04-6, "Accounting for Stripping Costs Incurred During Production in the Mining Industry." EITF 04-6 requires that stripping costs incurred during the production phase of a mine are to be accounted for as variable production costs that should be included in the costs of the inventory produced (that is, extracted) during the period that the stripping costs are incurred. Upon adoption, Alcoa recognized a cumulative effect adjustment in the opening balance of retained earnings of $3, representing the reduction in the net book value of post-production stripping costs of $8, offset by a related deferred tax liability of $3 and minority interests of $2.

D. Restructuring and Other Charges – In the first quarter of 2006, Alcoa recorded a net charge of $1 ($1 after tax and minority interests) for restructurings associated with previously approved restructuring programs.

For the full year 2005, Alcoa recorded charges of $292 ($190 after tax and minority interests) for restructuring and other items, resulting from the global realignment of Alcoa's organization structure. The 2005 charges were comprised of the following components: $238 of charges for employee termination and severance costs associated with approximately 8,450 salaried and hourly employees, spread globally across the company; $86 related to asset impairments for structures, machinery, and equipment; and $16 for exit costs, consisting primarily of accelerated depreciation associated with assets for which the useful life has been changed due to plans to close certain facilities in the near term. Reversals of previously recorded layoff and other costs of $48 were primarily due to Alcoa's decision to sell certain locations that it previously planned to shut down in 2005. The 2005 restructuring charges have been reclassified in 2006 to reflect the movement of the home exteriors business and the Hawesville, KY automotive casting facility to discontinued operations in 2006. Charges related to these businesses consisted of asset impairments of $45 and a charge of $2 for employee termination and severance costs associated with 183 people. As of March 31, 2006, approximately 4,800 of the 8,450 employees associated with the 2005 restructuring program had been terminated. Cash payments of approximately $23 were made against these reserves in the first quarter of 2006. Restructuring and other charges are not included in the segment results.

Activity and reserve balances for restructuring charges are as follows:

	Employee termination and severance costs	Other exit costs	Total
Reserve balances at December 31, 2004	$ 24	$ 39	$ 63
2005:			
Cash payments	(78)	(7)	(85)
2005 restructuring charges	238	6	244
Reversals of previously recorded restructuring charges	(48)	—	(48)
Reserve balances at December 31, 2005	$ 136	$ 38	$174
2006:			
Cash payments	(22)	(1)	(23)
2006 restructuring charges	1	2	3
Reversals of previously recorded restructuring charges	(4)	—	(4)
Reserve balances at March 31, 2006	$ 111	$ 39	$150

For further details on the 2005 restructurings, see Note D to the audited financial statements contained in the Annual Report on Form 10-K for the year ended December 31, 2005.

E. Pension Plans and Other Postretirement Benefits – The components of net periodic benefit cost follow.

	Pension benefits		Postretirement benefits	
First quarter ended March 31	2006	2005	2006	2005
Service cost	$ 52	$ 52	$ 8	$ 8
Interest cost	154	154	50	54
Expected return on plan assets	(185)	(177)	(4)	(4)
Amortization of prior service cost	3	6	2	1
Recognized actuarial loss	32	23	13	15
Net periodic benefit cost	$ 56	$ 58	$ 69	$ 74

The net periodic benefit cost for postretirement benefits for the first quarter of 2006 and 2005 reflects a reduction of approximately $13 and $6, respectively, in each year. This reduction is related to the recognition of the federal subsidy under Medicare Part D. For further details on the Medicare Part D subsidy, see Note W to the audited financial statements contained in the Annual Report on Form 10-K for the year ended December 31, 2005.

F. Other Income, Net

First quarter ended March 31	2006	2005
Equity income	$19	$35
Interest income	17	11
Foreign exchange gains (losses)	2	(5)
Other expense	(3)	(5)
	$35	$36

G. Income Taxes – The effective tax rate of 28.2% for the 2006 first quarter differs from the U.S. federal statutory rate of 35% due to income being taxed in lower rate jurisdictions. It also differs from the 2005 first quarter effective tax rate of 36.6% primarily due to the $43 income tax charge recorded in the first quarter of 2005 for previously undistributed equity earnings related to Alcoa's stake in Elkem ASA.

H. Discontinued Operations and Assets Held for Sale – In the third quarter of 2006, Alcoa reclassified its home exteriors business to discontinued operations upon the signing of a definitive sale agreement with Ply Gem Industries, Inc. In the first quarter of 2006, Alcoa reclassified the Hawesville, KY automotive

casting facility to discontinued operations upon closure of the facility. The condensed consolidated financial statements for all periods presented have been reclassified to reflect these businesses in discontinued operations. The operating results of the home exteriors business and the automotive casting facility are not included in the Extruded and End Products segment and the Engineered Solutions segment, respectively.

For the periods presented in the Condensed Consolidated Financial Statements, businesses classified as assets held for sale/discontinued operations included the home exteriors business, the telecommunications business, a small casting facility in Europe, the flexible packaging business in South America, and the Hawesville, KY automotive casting facility. The imaging and graphic communications business and the protective packaging business were also included in the first quarter 2005 results.

In the first quarter of 2006, Alcoa recorded a loss of $6 (after tax and minority interests) in discontinued operations, consisting of operating losses of $3 and a loss of $3 related to the 2005 sale of the imaging and graphic communications business. In the first quarter of 2005, Alcoa recorded a loss of $9 (after tax and minority interests) in discontinued operations, consisting of: a loss of $8 in connection with the divestiture of its interest in the AFL telecommunications business; a $4 impairment charge to reflect the estimated fair value of the protective packaging business and a small casting facility in Europe; and net operating income of $3.

The following table details selected financial information for the businesses included within discontinued operations.

First quarter ended March 31	2006	2005
Sales	$147	$303
(Loss) gain from operations	(4)	5
Loss on sale of businesses	(4)	(12)
Loss from impairment	—	(4)
Total pretax loss	$ (8)	$ (11)
Income tax benefit	2	—
Minority interests	—	2
Loss from discontinued operations	$ (6)	$ (9)

The major classes of assets and liabilities of operations held for sale in the balance sheet are as follows:

	March 31, 2006	December 31, 2005
Assets:		
Receivables	$ 100	$ 78
Inventories	47	61
Properties, plants, and equipment, net	57	63
Goodwill	37	37
Other assets	5	9
Total assets held for sale	$ 246	$ 248
Liabilities:		
Accounts payable, accrued expenses, and other	$ 94	$ 126
Total liabilities of operations held for sale	$ 94	$ 126

I. Earnings Per Share – The information used to compute basic and diluted EPS on income from continuing operations follows: (shares in millions)

First quarter ended March 31	2006	2005
Income from continuing operations	$614	$269
Less: preferred stock dividends	—	—
Income from continuing operations available to common shareholders	$614	$269
Average shares outstanding – basic	871	871
Effect of dilutive securities:		
Shares issuable upon exercise of dilutive stock options	5	8
Average shares outstanding – diluted	876	879

Options to purchase 60 million and 63 million shares of common stock at average exercise prices of $37.00 were outstanding as of March 31, 2006 and 2005, respectively, but were not included in the computation of diluted EPS because the option exercise price was greater than the average market price of the common shares.

J. Inventories

	March 31, 2006	December 31, 2005
Finished goods	$ 1,115	$ 962
Work in process	1,134	1,024
Bauxite and alumina	545	486
Purchased raw materials	704	691
Operating supplies	236	229
	$ 3,734	$ 3,392

Approximately 45% of total inventories at March 31, 2006, was valued on a LIFO basis. If valued on an average cost basis, total inventories would have been $914 and $858 higher at March 31, 2006, and December 31, 2005, respectively. The increase in the LIFO reserve resulted in a charge to cost of goods sold in the first quarter of 2006 of $56 ($36 after tax).

K. Commitments and Contingencies - Various lawsuits, claims and proceedings have been or may be instituted or asserted against Alcoa, including those pertaining to environmental, product liability, and safety and health matters. While the amounts claimed may be substantial, the ultimate liability cannot now be determined because of the considerable uncertainties that exist. Therefore, it is possible that results of operations or liquidity in a particular period could be materially affected by certain contingencies. However, based on facts currently available, management believes that the disposition of matters that are pending or asserted will not have a materially adverse effect on the financial position or liquidity of the company.

Alcoa Aluminio S.A. (Aluminio) is a participant in several hydroelectric power construction projects in Brazil for purposes of increasing its energy self-sufficiency and providing a long-term, low-cost source of power for its facilities. The Machadinho and Barra Grande projects have been completed.

Aluminio committed to taking a share of the output of the Machadinho project, completed in 2002, for 30 years at cost (including cost of financing the project). In the event that other participants in this project fail to fulfill their financial responsibilities, Aluminio may be required to fund a portion of the deficiency. In accordance with the agreement, if Aluminio funds any such deficiency, its participation and share of the output from the project will increase proportionately.

Barra Grande operations started up in November 2005 and full capacity was reached in February 2006. With Machadinho and Barra Grande, Aluminio's current power self-sufficiency is approximately 38%, to meet a total energy demand of approximately 690 megawatts from Brazilian primary plants. Aluminio accounts for the Machadinho and Barra Grande hydroelectric projects on the equity method. Its total investment in these projects was $161 and $152 at March 31, 2006 and December 31, 2005, respectively. Alcoa's maximum exposure to loss on these completed projects is $487, which represents Alcoa's investment and guarantees of debt.

In the first quarter of 2006, Aluminio acquired an additional 6.41% share in the Estreito hydroelectric power project, reaching 25.49% of total participation in the consortium. This additional share entitles Aluminio to 38 megawatts of assured energy. The project will have total installed capacity of 1,087 megawatts and assured power of 589 megawatts. In September 2005, the consortium submitted the necessary plans to obtain the environmental installation license, which is expected to be issued in April 2006 with start-up construction anticipated in June 2006.

In 2004, Alcoa agreed to acquire a 20% interest in a consortium formed to acquire the Dampier to Bunbury Natural Gas Pipeline (DBNGP) in Western Australia in exchange for an initial cash investment of $17, which was classified as an equity investment. Alcoa has made additional contributions of $23, including $4 in the first quarter of 2006, and committed to invest an additional $49 to be paid as the pipeline expands through 2008. The investment in the DBNGP was made in order to secure a competitively priced long-term supply of power to Alcoa's refineries in Western Australia. In addition to its equity ownership, Alcoa has an agreement to purchase gas transmission services from the DBNGP with the ability to terminate the agreement at its discretion. Alcoa's maximum exposure to loss on the investment and the related contract is approximately $300.

L. Comprehensive Income

First quarter ended March 31	2006	2005
Net income	$ 608	$260
Changes in other comprehensive income, net of tax:		
Unrealized gains (losses) on available-for-sale securities	169	(8)
Unrealized translation adjustments	34	(87)
Unrecognized (losses) gains on derivatives:		
Net change from periodic revaluations *	(141)	59
Net amount reclassified to income *	(35)	(16)
Net unrecognized (losses) gains on derivatives	(176)	43
Comprehensive income	$ 635	$208

* Prior period amounts have been reclassified to conform to current period presentation.

M. Segment Information – Alcoa's reportable segments, as reclassified for discontinued operations and assets held for sale, follow.

First quarter ended March 31, 2006	Alumina	Primary Metals	Flat-Rolled Products	Extruded and End Products	Engineered Solutions	Packaging and Consumer	Total
Sales:							
Third-party sales *	$ 628	$1,408	$ 1,940	$ 1,038	$ 1,360	$ 749	$7,123
Intersegment sales	555	1,521	49	23	—	—	2,148
Total sales	$1,183	$2,929	$ 1,989	$ 1,061	$ 1,360	$ 749	$9,271
Profit and loss:							
Equity (loss) income	$ (1)	$ 20	$ —	$ —	$ —	$ —	$ 19
Depreciation, depletion and amortization	43	96	50	28	40	31	288
Income taxes	93	197	26	1	37	5	359
ATOI	242	445	66	—	83	8	844
First quarter ended March 31, 2005							
Sales:							
Third-party sales *	$ 505	$1,089	$ 1,655	$ 915	$ 1,237	$ 708	$6,109
Intersegment sales	393	1,303	34	14	—	—	1,744
Total sales	$ 898	$2,392	$ 1,689	$ 929	$ 1,237	$ 708	$7,853
Profit and loss:							
Equity (loss) income	$ (1)	$ 18	$ —	$ —	$ 1	$ 1	$ 19
Depreciation, depletion and amortization	41	90	52	29	47	32	291
Income taxes	61	92	24	(2)	26	10	211
ATOI	161	225	75	11	61	16	549

* The difference between the segment total and consolidated third-party sales is in Corporate.

The following reconciles segment information to consolidated totals.

First quarter ended March 31	2006	2005
Total ATOI	$ 844	$549
Impact of LIFO and intersegment profit adjustments **	24	(2)
Unallocated amounts (net of tax):		
Interest income	11	7
Interest expense	(60)	(51)
Minority interests	(105)	(60)
Corporate expense	(89)	(69)
Restructuring and other charges	(1)	(30)
Discontinued operations	(6)	(9)
Other **	(10)	(75)
Consolidated net income	$ 608	$260

** Prior periods corporate LIFO expense has been reclassified from "Other" to combine the total impact of inventory related items.

The following table details segment assets.

	March 31, 2006	December 31, 2005
Alumina	$ 4,457	$ 4,268
Primary Metals	9,095	8,566
Flat-Rolled Products	4,627	3,963
Extruded and End Products	2,260	2,021
Engineered Solutions	5,932	5,733
Packaging and Consumer	2,832	2,787
Total segment assets ***	$ 29,203	$ 27,338

*** The difference between the segment total and consolidated assets is in Corporate.

N. Reclassifications - Certain amounts have been reclassified to conform to current period presentation.

Report of Independent Registered Public Accounting Firm*

To the Shareholders and Board of Directors of Alcoa Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Alcoa Inc. and its subsidiaries (Alcoa) as of March 31, 2006, and the related condensed statements of consolidated income and cash flows for the three-month periods ended March 31, 2006 and 2005. These interim financial statements are the responsibility of Alcoa's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2005, and the related statements of consolidated income, shareholders' equity and of cash flows for the year then ended, management's assessment of the effectiveness of Alcoa's internal control over financial reporting as of December 31, 2005 and the effectiveness of Alcoa's internal control over financial reporting as of December 31, 2005; and in our report dated February 17, 2006, except with respect to our opinion on the consolidated financial statements insofar as it relates to the effects of the discontinued operations discussed in Note B to those consolidated financial statements, as to which the date is January 15, 2007, we expressed unqualified opinions thereon. The consolidated financial statements and management's assessment of the effectiveness of internal control over financial reporting referred to above are not presented herein. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet information as of December 31, 2005, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP

Pittsburgh, Pennsylvania
April 26, 2006, except with respect to the effects of the discontinued operations discussed in Note H, as to which the date is January 15, 2007.

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* This report should not be considered a "report" within the meaning of Sections 7 and 11 of the 1933 Act and the independent accountant's liability under Section 11 does not extend to it.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(dollars in millions, except per share amounts and ingot prices; shipments in thousands of metric tons [mt])

Certain statements in this report under this caption and elsewhere relate to future events and expectations and, as such, constitute forward-looking statements. Forward-looking statements include those containing such words as "anticipates," "believes," "estimates," "expects," "hopes," "targets," "should," "will," "will likely result," "forecast," "outlook," "projects" or similar expressions. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of Alcoa to be different from those expressed or implied in the forward-looking statements. For a discussion of some of the specific factors that may cause such a difference, see Note K to the Condensed Consolidated Financial Statements; the disclosures included below under Segment Information, Environmental Matters, and Quantitative and Qualitative Disclosures about Market Risks; and Alcoa's Form 10-K, Part I, Item 1A, for the year ended December 31, 2005. Alcoa disclaims any intention or obligation (other than as required by law) to update or revise any forward-looking statements.

Results of Operations

***Selected Financial Data*:**

First quarter ended March 31	2006	2005
Sales	$7,111	$6,099
Income from continuing operations	614	269
Loss from discontinued operations	(6)	(9)
Net income	$ 608	$ 260
Earnings per common share:		
Diluted – Income from continuing operations	$ .70	$ .31
Diluted – Net income	$ .69	$ .30
Shipments of aluminum products (mt)	1,350	1,279
Shipments of alumina (mt)	2,023	1,923
Alcoa's average realized ingot price per metric ton	$2,534	$2,042
Average 3-month LME price per metric ton	$2,443	$1,887

Alcoa's income from continuing operations for the 2006 first quarter was $614, or 70 cents per diluted share, compared with $269, or 31 cents per share, in the first quarter of 2005. The increase of 128% was principally due to higher realized prices for alumina and aluminum which rose 22% and 24%, respectively, in the 2006 first quarter, compared with the corresponding period of 2005. Results in 2006 were also favorably impacted by higher volumes in five of Alcoa's six segments, as sales in the upstream businesses and in businesses serving the aerospace, distribution, building and construction, and commercial transportation markets increased. These positive impacts were partially offset by increased raw material and energy costs. The 2005 first quarter was negatively impacted by a $43 income tax impact on previously undistributed equity earnings related to Alcoa's stake in Elkem ASA and restructuring charges of $25.

Net income for the 2006 first quarter was $608, or 69 cents per share, compared with $260, or 30 cents per share, for the corresponding period of 2005. Discontinued operations included a loss of $6 in the first quarter of 2006, which consisted of operating losses of $3 and a loss of $3 related to the 2005 sale of the imaging and graphic communications business.

Sales for the first quarter of 2006 increased $1,012, or 17%, compared with the 2005 corresponding period. The increase in sales was driven by the following: higher realized prices for alumina and aluminum; higher prices in businesses serving the aerospace, building and construction, and commercial transportation markets; higher volumes in five of six segments; and increased sales related to metal purchased and subsequently resold. Partially offsetting these increases were unfavorable foreign currency exchange movements and the impact of the Eastalco smelter curtailment.

Cost of goods sold (COGS) as a percentage of sales was 75.2% for the first quarter of 2006, compared with 79.2% for the corresponding 2005 period. The largest factors in the improvement in this percentage were higher volumes and increased realized prices in conjunction with lower levels of energy and raw materials cost increases in the first quarter of 2006 compared with the 2005 first quarter.

Selling, general administrative, and other expenses (SG&A) increased $45 in the first quarter of 2006, compared with the corresponding period of 2005. The increase in the 2006 first quarter principally resulted from the recognition of expense related to stock-based compensation, as well as increased deferred compensation costs in 2006. SG&A as a percentage of sales decreased from 5.1% in the 2005 first quarter to 5.0% in the first quarter of 2006.

Restructuring and other charges resulted in a net charge of $1 ($1 after tax and minority interests), for restructurings associated with previously approved restructuring programs. In the first quarter of 2005, restructuring and other charges resulted in expense of $45 ($25 after tax and minority interests), consisting principally of $39 for employee termination and severance costs associated with 1,800 salaried and hourly employees (primarily in North America, Europe, and South America) and $7, primarily for asset write-downs. Approximately $23 of cash payments were made in the first quarter of 2006 related to prior year restructuring programs. Restructuring and other charges are not reflected in the segment results.

The pre-tax impact of allocating these amounts to the segment results would have been as follows:

First quarter ended March 31	2006	2005
Alumina	$ —	$ (2)
Primary Metals	—	(2)
Flat-Rolled Products	—	(4)
Extruded and End Products	(3)	(7)
Engineered Solutions	1	(17)
Packaging and Consumer	2	(12)
Segment total	—	(44)
Corporate	(1)	(1)
Total restructuring and other charges	$ (1)	$ (45)

Interest expense for the 2006 first quarter increased $14, or 18%, compared with the corresponding period in 2005, primarily due to higher average effective interest rates, somewhat offset by an increase in interest capitalized.

Other income remained relatively flat in the first quarter of 2006, as compared with the corresponding period of 2005. Equity income decreased $16 in the first quarter of 2006, primarily due to the 2005 sale of Alcoa’s interests in Elkem ASA and Integris Metals. This decrease was mostly offset by favorable foreign currency exchange movements, as the U.S. Dollar strengthened against the Australian Dollar and Brazilian Real, and an increase in interest income.

The effective tax rate of 28.2% for the 2006 first quarter differs from the U.S. federal statutory rate of 35% due to income being taxed in lower rate jurisdictions. It also differs from the 2005 first quarter effective tax rate of 36.6% primarily due to the $43 income tax charge recorded in the first quarter of 2005 for previously undistributed equity earnings related to Alcoa’s stake in Elkem ASA.

Minority interests’ share of income from operations increased $45, or 75%, in the 2006 first quarter, as compared with the 2005 corresponding period. The increase was principally due to higher earnings at Alcoa World Alumina and Chemicals (AWAC), as an increase in realized prices and higher volumes contributed to the increase in earnings.

The current master labor agreement between Alcoa and the United Steelworkers which covers approximately 9,000 U.S. employees across 15 locations expires on May 31, 2006. If an agreement is not reached, a work stoppage could occur. The segments that could be impacted in the event of a work stoppage include: Alumina, Primary Metals, Flat-Rolled Products, Extruded and End Products, and Packaging and Consumer. In the first quarter of 2006, Alcoa began to build targeted, strategic inventories to prepare for a potential work stoppage.

Segment Information

I. Alumina

First quarter ended March 31	2006	2005
Alumina production (mt)	3,702	3,583
Third-party alumina shipments (mt)	2,023	1,923
Third-party sales	$ 628	$ 505
Intersegment sales	555	393
Total sales	$1,183	$ 898
After-tax operating income (ATOI)	$ 242	$ 161

Third-party sales for the Alumina segment increased 24% in the 2006 first quarter, as compared with the corresponding 2005 period, primarily due to an increase in realized prices of 22% and increased volumes of 5% in the first quarter of 2006. Intersegment sales increased 41% in the 2006 first quarter, compared with the corresponding period of 2005, as a result of higher realized prices and higher volumes.

ATOI for this segment increased 50% in the 2006 first quarter, as compared with the first quarter of 2005, due to higher realized prices and increased volumes, somewhat offset by increased costs for raw materials and energy.

Realized alumina prices are expected to benefit from rising LME prices during the second quarter of 2006, and productivity gains are anticipated to continue. In addition, the Pinjarra expansion will be ramping up for production.

II. Primary Metals

First quarter ended March 31	2006	2005
Aluminum production (mt)	867	851
Third-party aluminum shipments (mt)	488	487
Alcoa's average realized price for aluminum ingot per metric ton	$2,534	$2,042
Third-party sales	$1,408	$1,089
Intersegment sales	1,521	1,303
Total sales	$2,929	$2,392
ATOI	$ 445	$ 225

Third-party sales for the Primary Metals segment increased 29% in the 2006 first quarter, as compared with the corresponding period of 2005. The increase is primarily due to higher realized prices of 24% in the 2006 first quarter, slightly offset by the loss of revenue from the curtailed Eastalco smelter. Intersegment sales increased 17% in the first quarter of 2006, primarily due to the increase in realized prices.

ATOI for this segment increased 98% in the 2006 first quarter, compared with the corresponding period in 2005 principally due to higher realized prices, higher volumes, and productivity gains. These positives were somewhat offset by increased costs for energy, raw materials, labor, and transportation.

Alcoa has approximately 509,000 metric tons per year (mtpy) of idle capacity on a base capacity of 4,066,000 mtpy. Base capacity increased by 62,000 mtpy in the first quarter of 2006 due to the completion of the Alumar expansion.

Alcoa will remain exposed to the higher LME prices in the second quarter. Energy costs are expected to remain a challenge in the second quarter. Alcoa will recognize the full benefit of the Alumar expansion, however, the Portland smelter will be operating at an average capacity of 94% in the second quarter.

III. Flat-Rolled Products

First quarter ended March 31	2006	2005
Third-party aluminum shipments (mt)	562	509
Third-party sales	$1,940	$1,655
Intersegment sales	49	34
Total sales	$1,989	$1,689
ATOI	$ 66	$ 75

Third-party sales for the Flat-Rolled Products segment increased 17% in the first quarter of 2006, as compared with the corresponding period of 2005. The increase resulted primarily from higher volumes, particularly at the Russian fabricating facilities that were acquired in January 2005; higher prices; and favorable mix for sheet and plate serving the aerospace market. These positive contributions were partially offset by unfavorable foreign currency exchange movements in Europe.

ATOI for this segment decreased 12% in the 2006 first quarter, compared with the corresponding period of 2005. The decrease was primarily due to higher energy and other input costs and operating losses associated with the Russian fabricating facilities. These negatives were somewhat offset by favorable mix for sheet and plate serving the aerospace market, productivity gains, higher prices, and higher volumes.

Demand is expected to remain strong in the aerospace and commercial transportation markets. Typical seasonal increases are anticipated in the can sheet business in the second quarter of 2006. Operations at the Russian facilities will continue to be challenging.

IV. Extruded and End Products

First quarter ended March 31	2006	2005
Third-party aluminum shipments (mt)	223	211
Third-party sales	$1,038	$915
Intersegment sales	23	14
Total sales	$1,061	$929
ATOI	$ —	$ 11

Third-party sales for the Extruded and End Products segment increased 13% in the 2006 first quarter, as compared with the 2005 corresponding period, principally due to higher prices and higher volumes in the businesses serving the building and construction market, slightly offset by unfavorable foreign currency exchange movements.

ATOI for this segment was at breakeven in the 2006 first quarter, as compared with ATOI of $11 in the corresponding period of 2005. The decline was primarily due to operating losses at the Russian facilities, higher raw materials costs, and pricing and productivity issues in the soft-alloy extrusion businesses, partially offset by higher prices and increased volumes in the businesses serving the building and construction market.

Seasonal increases in the building and construction businesses and increased demand for soft-alloy extrusions are anticipated in the second quarter. Demand is expected to remain strong in the aerospace and commercial transportation markets in the second quarter.

V. Engineered Solutions

First quarter ended March 31	2006	2005
Third-party aluminum shipments (mt)	37	38
Third-party sales	$1,360	$1,237
Intersegment sales	—	—
Total sales	$1,360	$1,237
ATOI	$ 83	$ 61

Third-party sales for the Engineered Solutions segment increased 10% in the 2006 first quarter, as compared with the 2005 corresponding period. The increase was principally due to higher volumes in the businesses serving the commercial transportation and aerospace markets. Favorable mix and the ability to pass through increased raw material costs also contributed to this increase.

ATOI for this segment increased 36% in the first quarter of 2006, as compared with the corresponding period of 2005. Increased volumes, improved productivity, and favorable price and mix positively impacted results. In addition, the 2005 portfolio restructuring resulted in improvement in the automotive business in the first quarter of 2006.

Demand in the aerospace and commercial transportation markets is expected to remain strong through the second quarter of 2006, while demand in the automotive market is expected to soften. The productivity gains realized in the first quarter are expected to continue through the second quarter of 2006.

VI. Packaging and Consumer

First quarter ended March 31	2006	2005
Third-party aluminum shipments (mt)	40	34
Third-party sales	$749	$708
Intersegment sales	—	—
Total sales	$749	$708
ATOI	$ 8	$ 16

Third-party sales for the Packaging and Consumer segment increased 6% in the 2006 first quarter, compared with the 2005 corresponding period. The increase was primarily due to increased volumes in the consumer products and closures businesses and higher prices, as Alcoa was able to pass through a portion of the increased resin costs. These positives were somewhat offset by a decrease in volumes and inability to pass through higher resin costs in the food packaging business.

ATOI for this segment declined 50% in the first quarter of 2006, compared with the corresponding period of 2005. The increases in prices and volumes noted previously, along with productivity gains, were more than offset by higher input costs, higher energy and transportation costs, and the inability to pass through higher resin costs in the food packaging business.

In the second quarter, seasonal strengthening in the consumer products and closures businesses is anticipated.

Reconciliation of ATOI to Consolidated Net Income

Items required to reconcile ATOI to consolidated net income include: certain effects of LIFO inventory accounting and intersegment profit adjustments; interest income and expense; minority interests; corporate expense, comprised of the general administrative and selling expenses of operating the corporate headquarters and other global administrative facilities along with depreciation and amortization on corporate-owned assets; restructuring and other charges; discontinued operations; and other, which includes the differences between estimated tax rates used in the segments and the corporate effective tax rate, and other nonoperating items such as foreign currency translation gains/losses.

The following reconciles segment information to consolidated totals.

First quarter ended March 31	2006	2005
Total ATOI	$ 844	$ 549
Impact of LIFO and intersegment profit adjustments *	24	(2)
Unallocated amounts (net of tax):		
Interest income	11	7
Interest expense	(60)	(51)
Minority interests	(105)	(60)
Corporate expense	(89)	(69)
Restructuring and other charges	(1)	(30)
Discontinued operations	(6)	(9)
Other *	(10)	(75)
Consolidated net income	$ 608	$ 260

* Prior periods corporate LIFO expense has been reclassified from "Other" to combine the total impact of inventory related items.

The significant changes in the reconciling items between ATOI and consolidated net income for the 2006 first quarter compared with the corresponding 2005 period consisted of:

- an increase in minority interests, due to an increase in earnings at Alcoa World Alumina and Chemicals (AWAC),
- an increase in corporate expenses, primarily due to increased stock-based compensation expenses,
- a decrease in restructuring and other charges due to the absence of new restructurings in the first quarter of 2006, and
- a decrease in other, primarily due to the 2005 first quarter $43 income tax impact of previously undistributed equity earnings related to Alcoa's stake in Elkem ASA.

The following table details segment assets.

	March 31, 2006	December 31, 2005
Alumina	$ 4,457	$ 4,268
Primary Metals	9,095	8,566
Flat-Rolled Products	4,627	3,963
Extruded and End Products	2,260	2,021
Engineered Solutions	5,932	5,733
Packaging and Consumer	2,832	2,787
Total segment assets **	$ 29,203	$ 27,338

** The difference between the segment total and consolidated assets is in Corporate.

The increase in segment assets across all segments in the first quarter of 2006 was due to higher customer receivables and increased inventories from improved market conditions and the strategic, targeted building of inventory in preparation for a potential work stoppage.

Statement of Financial Position

Comprehensive income was $635 in the first quarter ended March 31, 2006, which consisted primarily of $608 in net income for the first quarter; a $169 increase in the unrealized gain on available-for-sale securities; a $34 increase in unrealized translation adjustments due to the strengthening of the U.S. Dollar against the Australian Dollar and Brazilian Real; somewhat offset by a $176 increase in net unrecognized losses on derivatives, principally due to the decrease in the fair value of certain cash flow hedges.

Liquidity and Capital Resources

Cash from Operations

Cash used for operations was $213 in the 2006 first quarter compared with cash used for operations of $239 in the same period of 2005. The change of $26 is principally due to the $348 increase in net income and the $93 long-term aluminum supply contract entered into during the first quarter of 2005. These items were mostly offset by a net increase in working capital of $387, including a net decrease in payables of $361 and a $92 net decrease in accrued taxes, primarily due to the payment of an Australian stamp tax.

Financing Activities

Cash provided from financing activities was $570 in the 2006 first quarter, a change of $299 compared with cash from financing activities of $869 in the corresponding period of 2005. The change was primarily due to a $242 decrease in the net change in commercial paper, as less commercial paper was issued in the first quarter of 2006 compared with the first quarter of 2005, and the $60 repurchase of common stock in the first quarter of 2006 to offset the dilutive effect associated with stock option exercises.

Investing Activities

Cash used for investing activities was $667 in the 2006 first quarter compared with $584 in the first quarter of 2005. The change of $83 was primarily due to the following:

- a $245 increase in capital expenditures related to several growth projects, including the construction of the Iceland smelter and an anode facility in Norway,
- a $52 net increase in short-term investments and restricted cash, primarily due to funding requirements related to joint ventures in China,
- the absence of cash proceeds of $206 related to the sale of Alcoa's interest in Integris Metals in the first quarter of 2005, and
- the absence of cash outlays of $432 for acquisitions that occurred in the first quarter of 2005 and principally consisted of cash paid of $257 for two Russian fabricating facilities and the $176 cash payment associated with the acquisition of full ownership of the AFL automotive business.

Critical Accounting Policies and Estimates

On January 1, 2006, Alcoa adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), "Share-Based Payment," which requires the company to recognize compensation expense for stock-based compensation based on the fair value of the share-based employee grants. SFAS No. 123(R) revises SFAS No. 123 "Accounting for Stock-Based Compensation" and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Alcoa elected the modified prospective application method for adoption, and prior periods financial statements have not been restated.

Alcoa recognizes compensation expense for employee equity grants using the non-substantive vesting period approach, in which the expense (net of estimated forfeitures) is recognized ratably over the requisite service period following the date of grant. Prior to the adoption of SFAS No. 123(R), Alcoa used the nominal vesting approach related to retiree-eligible employees, in which the compensation expense is recognized ratably over the original vesting period. As part of Alcoa's stock-based compensation plan design, individuals that are retirement-eligible have a six-month requisite service period in the year of grant. Equity grants are issued in early January each year. As a result, a larger portion of expense will be recognized in the first and second quarters of each year for these retiree-eligible employees. First quarter compensation expense was $28 ($20 after tax). Of this amount, $20 pertains to retirement-eligible employees.

As of January 1, 2005, Alcoa switched from the Black-Scholes pricing model to a lattice model to estimate fair value at grant date for future option grants. On December 31, 2005, Alcoa accelerated the vesting of 11 million unvested stock options granted to employees in 2004 and on January 13, 2005. The 2004 and 2005 accelerated options had weighted average exercise prices of $35.60 and $29.54, respectively, and in the aggregate represented approximately 12 percent of Alcoa's total outstanding options. The decision to accelerate the vesting of the 2004 and 2005 options was made primarily to avoid recognizing the related compensation expense in future financial statements upon the adoption of SFAS No. 123(R). Alcoa expects the accelerated vesting of the 2004 and 2005 stock options to reduce its after-tax stock option compensation expense by $21 in 2006 and by $7 in 2007.

An additional change has been made to the stock-based compensation program for 2006 grants. Plan participants can choose whether to receive their award in the form of stock options, restricted stock units (stock awards), or a combination of both. This choice is made before the grant is issued and is irrevocable. This choice resulted in an increased stock award expense in comparison to 2005.

SFAS No. 123(R) requires Alcoa to recognize compensation expense for stock-based compensation ratably over the requisite service period based on the fair value of the grant. Determining the fair value of stock options at grant date requires judgment including estimates for the average risk-free interest rate, expected volatility, expected exercise behavior, expected dividend yield, and expected forfeitures. If any of these assumptions differ significantly from actual, stock-based compensation expense could be impacted. Prior to the adoption of SFAS No. 123(R), the company accounted for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations using the intrinsic value method, which resulted in no compensation cost for options granted.

Recently Adopted Accounting Standards

Effective January 1, 2006, Alcoa adopted Emerging Issues Task Force (EITF) Issue No. 04-6, "Accounting for Stripping Costs Incurred During Production in the Mining Industry." EITF 04-6 requires that stripping costs incurred during the production phase of a mine are to be accounted for as variable production costs that should be included in the costs of the inventory produced (that is, extracted) during the period that the stripping costs are incurred. Upon adoption, Alcoa recognized a cumulative effect adjustment in the opening balance of retained earnings of $3, representing the reduction in the net book value of post-production stripping costs of $8, offset by a related deferred tax liability of $3 and minority interests of $2.

Environmental Matters

Alcoa continues to participate in environmental assessments and cleanups at a number of locations. These include approximately 37 owned or operating facilities and adjoining properties, approximately 34 previously owned or operating facilities and adjoining properties and approximately 64 waste sites, including Superfund sites. A liability is recorded for environmental remediation costs or damages when a cleanup program becomes probable and the costs or damages can be reasonably estimated.

As assessments and cleanups proceed, the liability is adjusted based on progress made in determining the extent of remedial actions and related costs and damages. The liability can change substantially due to factors such as the nature and extent of contamination, changes in remedial requirements, and technological changes. Therefore, it is not possible to determine the outcomes or to estimate with any degree of accuracy the potential costs for certain of these matters.

The following discussion provides additional details regarding the current status of Alcoa's significant sites where the final outcome cannot be determined or the potential costs in the future cannot be estimated.

Massena, NY. Alcoa has been conducting investigations and studies of the Grasse River, adjacent to Alcoa's Massena, New York plant site, under order from the U.S. Environmental Protection Agency (EPA) issued under the Comprehensive Environmental Response, Compensation and Liability Act, also known as Superfund. Sediments and fish in the river contain varying levels of polychlorinated biphenyl (PCB).

In 2002, Alcoa submitted an Analysis of Alternatives Report that detailed a variety of remedial alternatives with estimated costs ranging from $2 to $525. Because the selection of the $2 alternative (natural recovery) was considered remote, Alcoa adjusted the reserve for the Grasse River in 2002 to $30 representing the low end of the range of possible alternatives, as no single alternative could be identified as more probable than the others.

In June of 2003, based on river observations during the spring of 2003, the EPA requested that Alcoa gather additional field data to assess the potential for sediment erosion from winter river ice formation and breakup. The results of these additional studies, submitted in a report to the EPA in April of 2004, suggest that this phenomenon has the potential to occur approximately every 10 years and may impact sediments in certain portions of the river under all remedial scenarios. The EPA informed Alcoa that a final remedial decision for the river could not be made without substantially more information, including river pilot studies on the effects of ice formation and breakup on each of the remedial techniques. Alcoa submitted to the EPA and the EPA approved a Remedial Options Pilot Study (ROPS) to gather this information. The scope of this study includes sediment removal and capping, the installation of an ice control structure, and significant monitoring.

In May of 2004, Alcoa agreed to perform the study at an estimated cost of $35. Most of the construction work has been completed in 2005 with monitoring proposed for 2006. The findings will be incorporated into a revised Analysis of Alternatives Report, which is expected to be submitted in 2007. This information will be used by the EPA to propose a remedy for the entire river.

Alcoa adjusted the reserves in the second quarter of 2004 to include the $35 for the ROPS. This is in addition to the $30 previously reserved. With the exception of the natural recovery remedy, none of the existing alternatives in the 2002 Analysis of Alternatives Report is more probable than the others and the results of the ROPS are necessary to revise the scope and estimated cost of many of the current alternatives.

The EPA's ultimate selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA's Record of Decision is issued, which is expected in 2007 or later.

Sherwin, TX. In connection with the sale of the Sherwin alumina refinery in Texas, which was required to be divested as part of the Reynolds merger in 2000, Alcoa has agreed to retain responsibility for the remediation of then existing environmental conditions, as well as a pro rata share of the final closure of the active waste disposal areas, which remain in use. Alcoa's share of the closure costs is proportional to the total period of operation of the active waste disposal areas. Alcoa estimated its liability for the active disposal areas by making certain assumptions about the period of operation, the amount of material placed in the area prior to closure, and the appropriate technology, engineering, and regulatory status applicable to final closure. The most probable cost for remediation has been reserved. It is reasonably possible that an additional liability, not expected to exceed $75, may be incurred if actual experience varies from the original assumptions used.

East St. Louis, IL. In response to questions regarding environmental conditions at the former East St. Louis, IL operations, Alcoa entered into an administrative order with the EPA in December 2002 to perform a remedial investigation and feasibility study of an area used for the disposal of bauxite residue from historic alumina refining operations. A draft feasibility study was submitted to the EPA in April 2005. The feasibility study includes remedial alternatives that range from no further action at $0 to significant grading, stabilization, and water management of the bauxite residue disposal areas at $75. Because the selection of the $0 alternative was considered remote, Alcoa increased the environmental reserve for this location by $15 in the second quarter of 2005, representing the low end of the range of possible alternatives which meets the remedy selection criteria, as no alternative could be identified as more probable than the others. The EPA has not completed a final review of the feasibility study and the EPA's selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA's Record of Decision is issued.

Based on the foregoing, it is possible that Alcoa's results of operations, in a particular period, could be materially affected by matters relating to these sites. However, based on facts currently available, management believes that adequate reserves have been provided and that the disposition of these matters will not have a materially adverse effect on the financial position or liquidity of the company.

Alcoa's remediation reserve balance was $360 and $390 at March 31, 2006 and December 31, 2005 (of which $39 and $40 was classified as a current liability), respectively, and reflects the most probable costs to remediate identified environmental conditions for which costs can be reasonably estimated. In the first quarter of 2006, the remediation reserve was decreased by approximately $17 primarily due to an adjustment for the liabilities at Russian fabricating facilities acquired in January 2005. This adjustment was made after further investigations were completed whereby Alcoa was able to obtain additional information about the environmental condition and the associated liabilities with these facilities. This adjustment was recorded as an opening balance sheet adjustment and had no impact on net income. Payments related to remediation expenses were approximately $13 in the first quarter of 2006. These amounts include expenditures currently mandated, as well as those not required by any regulatory authority or third party.

Included in annual operating expenses are the recurring costs of managing hazardous substances and environmental programs. These costs are estimated to be about 2% of cost of goods sold.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

In addition to the risks inherent in its operations, Alcoa is exposed to financial, market, political and economic risks. The following discussion provides information regarding Alcoa's exposure to the risks of changing commodity prices, foreign exchange rates, and interest rates.

Alcoa's derivative activities are subject to the management, direction, and control of the Strategic Risk Management Committee (SRMC). The SRMC is composed of the chief executive officer, the chief financial officer, and other officers and employees that the chief executive officer selects. The SRMC reports to the Board of Directors on the scope of its activities.

The interest rate, foreign currency, aluminum and other commodity contracts are held for purposes other than trading. They are used primarily to mitigate uncertainty and volatility, and to cover underlying exposures. The company is not involved in energy-trading activities, weather derivatives, or other nonexchange commodity-trading activities.

Commodity Price Risks – Alcoa is a leading global producer of primary aluminum products and aluminum fabricated products. As a condition of sale, customers often require Alcoa to enter into long-term, fixed-price commitments. These commitments expose Alcoa to the risk of higher aluminum prices between the time the order is committed and the time that the order is shipped. Alcoa also sells aluminum products to third parties at then-current market prices and is exposed to the risk of lower market prices at the time of shipment. Alcoa uses futures and option contracts, totaling approximately 653,000 mt at March 31, 2006, to reduce the aluminum price risk of these exposures. The effects of this hedging activity will be recognized in earnings over the designated hedge periods, generally within three years.

Alcoa has also entered into futures and option contracts, totaling approximately 150,000 metric tons at March 31, 2006, to hedge a portion of future production. The effect of this hedging activity will be recognized in earnings over the designated hedge periods in 2007 and 2008.

Alcoa has also entered into certain derivatives to minimize its price risk related to other customer sales and pricing arrangements. Alcoa has not qualified these contracts for hedge accounting treatment, and therefore, the fair value gains and losses on these contracts are recorded in earnings. These contracts totaled 32,000 mt at March 31, 2006. In addition, Alcoa has entered into power supply contracts that contain pricing provisions related to the LME aluminum price. The LME-linked pricing features are considered embedded derivatives. A majority of these embedded derivatives have been designated as hedges of future sales of aluminum. Gains and losses on the remainder of these embedded derivatives are recognized in earnings.

The net mark-to-market pre-tax earnings impact from aluminum derivative and hedging activities was a loss of approximately $18 in the 2006 first quarter. The loss was principally due to an embedded LME derivative in a power contract.

Alcoa purchases natural gas, fuel oil, and electricity to meet its production requirements and believes it is highly likely that such purchases will continue in the future. These purchases expose the company to the risk of higher prices. To hedge a portion of these risks, Alcoa uses futures and forward contracts. The effects of this hedging activity will be recognized in earnings over the designated hedge periods, generally within three years.

Financial Risk

Interest rates – Alcoa uses interest rate swaps to help maintain a strategic balance between fixed- and floating-rate debt and to manage overall financing costs. For a portion of its fixed-rate debt, the company has entered into pay floating, receive fixed interest rate swaps to effectively change the fixed interest rates to floating interest rates.

Currencies – Alcoa is subject to exposure from fluctuations in foreign currency exchange rates. Foreign currency exchange contracts may be used from time to time to hedge the variability in cash flows from the forecasted payment or receipt of currencies other than the functional currency. These contracts cover periods consistent with known or expected exposures, generally not exceeding three years.

Fair values – The following table shows the fair values of outstanding derivatives contracts at March 31, 2006.

	Fair value gain/(loss)
Aluminum	$ (80)
Interest rates	(154)
Other commodities, principally natural gas	52
Currencies	96

Aluminum consists of hedge contracts with gains of $284. These gains are more than offset by losses on embedded derivatives in power contracts in Iceland and Brazil and our share of losses on hedge contracts of Norwegian smelters that are accounted for under the equity method.

Material Limitations - The disclosures with respect to commodity prices, interest rates, and foreign exchange risk do not take into account the underlying commitments or anticipated transactions. If the underlying items were included in the analysis, the gains or losses on the futures contracts may be offset. Actual results will be determined by a number of factors that are not under Alcoa's control and could vary significantly from those factors disclosed.

Alcoa is exposed to credit loss in the event of nonperformance by counterparties on the above instruments, as well as credit or performance risk with respect to its hedged customers' commitments. Although nonperformance is possible, Alcoa does not anticipate nonperformance by any of these parties. Futures contracts are with creditworthy counterparties and are further supported by cash, treasury bills, or irrevocable letters of credit issued by carefully chosen banks. In addition, various master netting arrangements are in place with each counterparty to facilitate settlement of gains and losses on these contracts.

Item 4. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures

Alcoa’s Chief Executive Officer and Chief Financial Officer have evaluated the company’s disclosure controls and procedures as of the end of the period covered by this report, and they have concluded that these controls and procedures are effective.

(b) Changes in Internal Control Over Financial Reporting

There have been no changes in Alcoa’s internal control over financial reporting during the three-month period ended March 31, 2006, that have materially affected, or are reasonably likely to materially affect, the registrant’s internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

On January 6, 2006**,** Billy Musgrave, Jr. and Kim Musgrave, on behalf of themselves and all persons similarly situated, brought an action against Alcoa Inc. and Alcoa Fuels, Inc. in the Circuit Court of Warrick County, Indiana. The lawsuit alleges harm from exposure to toxic waste that was disposed in designated pits at the Squaw Creek Mine during the period from 1965 to 1979. The complaint seeks certification of a class of plaintiffs and recovery for compensatory and punitive damages, although plaintiffs do not specify in the complaint the amount sought in damages. Any result of this suit is at this time neither estimable nor probable.

As previously reported, the issuance of an Environmental Operating Permit (EOP) for the 346,000 mtpy Fjarðaál Project in Iceland was challenged, and in June 2005, the Icelandic Supreme Court ruled that a new Environmental Impact Assessment (EIA) should have been required by the Icelandic Planning Agency (PA) and Ministry of Environment, rather than the comparison study process that was followed. At the same time, the Court dismissed plaintiff's claims that the EOP should be invalidated. Construction has continued on the Project under previously-issued building permits, and on April 7, 2006, Alcoa submitted its new EIA to the PA. Alcoa expects the EIA process to be finished early in the third quarter of 2006, and a new EOP to be issued in the fourth quarter of 2006.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

(c) Issuer Purchases of Equity Securities:

Period	Total Number of Shares Purchased (a)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Repurchase Plans or Programs (b)	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs (b)
January 1 - January 31, 2006	48,982	$30.24	—	26,200,282
February 1 - February 28, 2006	1,479,800	$30.03	1,479,800	24,720,482
March 1 - March 31, 2006	528,412	$29.90	520,200	24,200,282
Total for quarter ended March 31, 2006	2,057,194	$30.00	2,000,000	24,200,282

(a) This column includes (i) purchases under Alcoa's publicly announced share repurchase program described in (b) below and (ii) the deemed surrender to the company by plan participants of shares of common stock to satisfy the exercise price related to the exercise of employee stock options, in each case to the extent applicable during the period indicated. The shares used to satisfy the exercise price related to stock options are not considered part of the publicly announced share repurchase program approved by Alcoa's Board of Directors as described in (b) below.

(b) Alcoa's share repurchase program was approved by Alcoa's Board of Directors and publicly announced on July 13, 2001. The program authorizes the repurchase of up to 50 million shares of Alcoa common stock from time to time, directly or through brokers or agents, and has no expiration date.

In addition to the 2 million shares purchased in the first quarter of 2006, Alcoa purchased 2 million shares of stock in April of 2006 for approximately $68 million, at an average price per share of $33.90, to replenish treasury stock shares that were issued from stock option exercises.

Item 4. Submission of Matters to a Vote of Security Holders.

Alcoa's annual meeting of shareholders was held on April 21, 2006. At the meeting:

(1) the three nominees named in Alcoa's 2006 proxy statement, Kathryn S. Fuller, Judith M. Gueron, and Ernesto Zedillo, were elected to serve as directors for a three-year term expiring in 2009; and

(2) the selection of PricewaterhouseCoopers LLP to serve as the independent auditor of Alcoa for 2006 was ratified.

The number of votes cast for, against or withheld, and the number of abstentions and broker non-votes, where applicable, as to each such matter, are set forth below.

	For	Against/ Withheld	Abstained	Broker Non-Votes
(1) Election of Directors:				
NOMINEE				
Kathryn S. Fuller	734,655,025	23,100,185		
Judith M. Gueron	729,740,260	28,014,950		
Ernesto Zedillo	733,246,898	24,508,312		
(2) Ratification of the Independent Auditor	736,522,822	9,739,574	11,492,611	203

Item 6. Exhibits.

12. Computation of Ratio of Earnings to Fixed Charges
31. Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32. Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

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

Alcoa Inc.

April 26, 2006	By	/s/ JOSEPH C. MUSCARI
Date		Joseph C. Muscari Executive Vice President and Chief Financial Officer (Principal Financial Officer)
April 26, 2006	By	/s/ CHARLES D. MCLANE, JR.
Date		Charles D. McLane, Jr. Vice President - Corporate Controller (Principal Accounting Officer)

EXHIBITS

12. Computation of Ratio of Earnings to Fixed Charges
31. Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32. Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

EXHIBIT 12

Alcoa and subsidiaries

Computation of Ratio of Earnings to Fixed Charges
For the three months ended March 31, 2006
(in millions, except ratio)

Three months ended March 31	2006
Earnings:	
Income from continuing operations before taxes on income	$1,001
Minority interests' share of earnings of majority-owned subsidiaries without fixed charges	—
Equity income	(19)
Fixed charges	104
Distributed income of less than 50%-owned persons	11
Amortization of capitalized interest	6
Total earnings	$1,103
Fixed Charges:	
Interest expense:	
Consolidated	$ 92
Proportionate share of 50%-owned persons	1
	$ 93
Amount representative of the interest factor in rents:	
Consolidated	$ 11
Proportionate share of 50%-owned persons	—
	$ 11
Fixed charges added to earnings	$ 104
Interest capitalized:	
Consolidated	$ 25
Proportionate share of 50%-owned persons	—
	$ 25
Preferred stock dividend requirements of majority-owned subsidiaries	—
Total fixed charges	$ 129
Ratio of earnings to fixed charges	8.6

EXHIBIT 31

Certifications

I, Alain J. P. Belda, Chairman of the Board and Chief Executive Officer of Alcoa Inc., certify that:

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

Date: April 26, 2006

/s/ ALAIN J. P. BELDA

Title: Chairman of the Board and
Chief Executive Officer

I, Joseph C. Muscari, Executive Vice President and Chief Financial Officer of Alcoa Inc., certify that:

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

Date: April 26, 2006

/s/ JOSEPH C. MUSCARI

Title: Executive Vice President and
Chief Financial Officer

EXHIBIT 32

Certification
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), each of the undersigned officers of Alcoa Inc., a Pennsylvania corporation (the "Company"), does hereby certify that:

The Quarterly Report on Form 10-Q for the quarter ended March 31, 2006 (the "Form 10-Q") of the Company fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: April 26, 2006

/s/ ALAIN J. P. BELDA
Name: Alain J. P. Belda
Title: Chairman of the Board and Chief Executive Officer

Dated: April 26, 2006

/s/ JOSEPH C. MUSCARI
Name: Joseph C. Muscari
Title: Executive Vice President and Chief Financial Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished to the Securities and Exchange Commission as an exhibit to the Form 10-Q and shall not be considered filed as part of the Form 10-Q.

PART I – FINANCIAL INFORMATION
Item 1. – Financial Statements.

Alcoa and subsidiaries
Condensed Consolidated Balance Sheet (unaudited)
(in millions)

	June 30 2006	December 31 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 453	$ 762
Receivables from customers, less allowances of $82 in 2006 and $75 in 2005	3,539	2,860
Other receivables	370	427
Inventories (J)	4,042	3,392
Fair value of derivative contracts	345	520
Prepaid expenses and other current assets	989	713
Total current assets	9,738	8,674
Properties, plants, and equipment, at cost	28,209	26,769
Less: accumulated depreciation, depletion, and amortization	14,223	13,661
Net properties, plants, and equipment	13,986	13,108
Goodwill	6,259	6,212
Investments	1,411	1,370
Other assets	4,126	4,084
Assets held for sale (H)	251	248
Total assets	$35,771	$ 33,696
LIABILITIES		
Current liabilities:		
Short-term borrowings	$ 361	$ 300
Commercial paper	1,898	912
Accounts payable, trade	2,730	2,570
Accrued compensation and retirement costs	1,011	1,096
Taxes, including taxes on income	945	871
Other current liabilities	1,086	1,445
Long-term debt due within one year	62	58
Total current liabilities	8,093	7,252
Long-term debt, less amount due within one year	5,158	5,279
Accrued pension benefits	1,464	1,500
Accrued postretirement benefits	2,111	2,105
Other noncurrent liabilities and deferred credits	2,089	1,821
Deferred income taxes	833	875
Liabilities of operations held for sale (H)	129	126
Total liabilities	19,877	18,958
MINORITY INTERESTS	1,474	1,365
COMMITMENTS AND CONTINGENCIES (K)		
SHAREHOLDERS' EQUITY		
Preferred stock	55	55
Common stock	925	925
Additional capital	5,807	5,720
Retained earnings	10,431	9,345
Treasury stock, at cost	(1,952)	(1,899)
Accumulated other comprehensive loss (L)	(846)	(773)
Total shareholders' equity	14,420	13,373
Total liabilities and equity	$35,771	$ 33,696

The accompanying notes are an integral part of the condensed consolidated financial statements.

Alcoa and subsidiaries
Condensed Statement of Consolidated Income (unaudited)
(in millions, except per-share amounts)

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Sales (M)	$ 7,797	$ 6,532	$14,908	$12,631
Cost of goods sold	5,827	5,275	11,171	10,103
Selling, general administrative, and other expenses	354	333	709	643
Research and development expenses	50	47	97	92
Provision for depreciation, depletion, and amortization	324	312	630	622
Restructuring and other charges (D)	(9)	214	(8)	259
Interest expense	98	87	190	165
Other income, net (F)	(61)	(347)	(96)	(383)
Total costs and expenses	6,583	5,921	12,693	11,501
Income from continuing operations before taxes on income	1,214	611	2,215	1,130
Provision for taxes on income (G)	341	61	623	251
Income from continuing operations before minority interests' share	873	550	1,592	879
Less: Minority interests' share	124	60	229	120
Income from continuing operations	749	490	1,363	759
Loss from discontinued operations (H)	(5)	(30)	(11)	(39)
NET INCOME	$ 744	$ 460	$ 1,352	$ 720
EARNINGS (LOSS) PER SHARE (I)				
Basic:				
Income from continuing operations	$ .86	$ .56	$ 1.57	$ .87
Loss from discontinued operations	(.01)	(.03)	(.02)	(.04)
Net income	$ .85	$ .53	$ 1.55	$ .83
Diluted:				
Income from continuing operations	$ .85	$ .56	$ 1.55	$ .86
Loss from discontinued operations	—	(.04)	(.01)	(.04)
Net income	$ .85	$ .52	$ 1.54	$ .82
Dividends paid per common share	$ .15	$ .15	$ .30	$ .30

The accompanying notes are an integral part of the condensed consolidated financial statements.

Alcoa and subsidiaries
Condensed Statement of Consolidated Cash Flows (unaudited) (in millions)

	Six months ended June 30	
	2006	2005
CASH FROM OPERATIONS		
Net income	$ 1,352	$ 720
Adjustments to reconcile net income to cash from operations:		
Depreciation, depletion, and amortization	631	623
Deferred income taxes	(3)	(102)
Equity (income) loss, net of dividends	(42)	64
Restructuring and other charges (D)	(8)	259
Gains from investing activities – sale of assets	(8)	(342)
Provision for doubtful accounts	10	9
Loss from discontinued operations (H)	11	39
Minority interests	229	120
Stock-based compensation (B)	50	12
Excess tax benefits from share-based payment arrangements	(15)	—
Other	(66)	(59)
Changes in assets and liabilities, excluding effects of acquisitions and divestitures:		
Increase in receivables	(491)	(604)
Increase in inventories	(569)	(445)
Increase in prepaid expenses and other current assets	(130)	(25)
(Decrease) increase in accounts payable and accrued expenses	(378)	70
Increase (decrease) in taxes, including taxes on income	29	6
Cash paid on long-term aluminum supply contract	—	(93)
Pension contributions	(102)	(46)
Net change in noncurrent assets and liabilities	(8)	(20)
CASH PROVIDED FROM CONTINUING OPERATIONS	492	186
CASH USED FOR DISCONTINUED OPERATIONS	(6)	(41)
CASH FROM OPERATIONS	486	145
FINANCING ACTIVITIES		
Net changes to short-term borrowings	54	(9)
Common stock issued for stock compensation plans	136	17
Repurchase of common stock	(210)	—
Dividends paid to shareholders	(262)	(263)
Dividends paid to minority interests	(200)	(72)
Net change in commercial paper	986	475
Additions to long-term debt	8	200
Payments on long-term debt	(27)	(47)
Excess tax benefits from share-based payment arrangements	15	—
Other	40	—
CASH PROVIDED FROM FINANCING ACTIVITIES	540	301
INVESTING ACTIVITIES		
Capital expenditures	(1,318)	(825)
Capital expenditures of discontinued operations	(3)	(9)
Acquisition of minority interests	(1)	(176)
Acquisitions, net of cash acquired	8	(257)
Sale of investments	7	1,077
Change in short-term investments and restricted cash	(21)	(228)
Additions to investments	(44)	(10)
Other	20	(9)
CASH USED FOR INVESTING ACTIVITIES	(1,352)	(437)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	17	(9)
Net change in cash and cash equivalents	(309)	—
Cash and cash equivalents at beginning of year	762	457
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 453	$ 457

The accompanying notes are an integral part of the condensed consolidated financial statements.

Notes to the Condensed Consolidated Financial Statements (unaudited)
(dollars in millions, except per-share amounts)

A. **Basis of Presentation** - The Condensed Consolidated Financial Statements are unaudited. These statements include all adjustments, consisting of normal recurring adjustments, considered necessary by management to fairly state the results of operations, financial position, and cash flows. The results reported in these Condensed Consolidated Financial Statements are not necessarily indicative of the results that may be expected for the entire year. The year-end balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

This Form 10-Q report should be read in conjunction with Alcoa's Annual Report on Form 10-K for the year ended December 31, 2005, which includes all disclosures required by accounting principles generally accepted in the United States of America.

B. Stock-Based Compensation – On January 1, 2006, Alcoa adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), "Share-Based Payment," which requires the company to recognize compensation expense for stock-based compensation based on the grant date fair value. This expense must be recognized ratably over the requisite service period following the date of grant. Alcoa has elected the modified prospective application method for adoption, and prior period financial statements have not been restated. Prior to January 1, 2006, Alcoa accounted for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations.

Stock options under Alcoa's stock-based compensation plans have been granted at not less than market prices on the dates of grant. Beginning in 2006, performance stock options were granted to certain individuals. The final number of options granted is based on the outcome of Alcoa's annual return on capital results against the results of a comparator group of companies. However, an individual can earn a minimum number of options if Alcoa's return on capital meets or exceeds its cost of capital. Stock option features based on date of original grant are as follows:

Date of original grant	Vesting	Term	Reload feature
2002 and prior	One year	10 years	One reload over option term
2003	3 years (1/3 each year)	10 years	One reload in 2004 for 1/3 vesting in 2004
2004 and forward	3 years (1/3 each year)	6 years	None

In addition to the stock options described above, Alcoa granted restricted stock units (stock awards) that vest in three years from the date of grant. Certain of these stock awards were granted with the same performance conditions described above for performance stock options.

The following table summarizes the total compensation expense recognized for all options and stock awards:

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Compensation expense reported in income:				
Stock option grants	$ 3	$ —	$ 6	$ —
Stock award grants	19	7	44	12
Total compensation expense before income taxes	22	7	50	12
Income tax benefit	9	2	17	4
Total compensation expense, net of income tax benefit	$ 13	$ 5	$ 33	$ 8

Prior to January 1, 2006, no stock-based compensation expense was recognized for stock options. As a result of the implementation of SFAS No. 123(R), Alcoa recognized additional compensation expense of $3 pre-tax ($2 after tax) and $6 pre-tax ($4 after tax) in the 2006 second quarter and six-month periods, respectively, which resulted in no impact on earnings per share. There were no stock-based

compensation expenses capitalized in the first six months of 2006 or 2005. Alcoa's net income and earnings per share for 2005 would have been reduced to the pro forma amounts shown below if employee stock option compensation expense had been determined based on the fair value at the grant dates in accordance with SFAS No. 123, "Accounting for Stock-Based Compensation," and SFAS No. 148, "Accounting for Stock-Based Compensation—Transition and Disclosure an amendment of FASB Statement No. 123."

	Second quarter ended June 30, 2005	Six months ended June 30, 2005
Net income, as reported	$ 460	$ 720
Add: compensation expense reported in net income, net of income tax	—	—
Less: compensation expense determined under the fair value method, net of income tax	9	18
Pro forma net income	$ 451	$ 702
Basic earnings per share:		
As reported	$ .53	$ .83
Pro forma	.52	.80
Diluted earnings per share:		
As reported	$ .52	$ .82
Pro forma	.51	.80

As of January 1, 2005, Alcoa switched from the Black-Scholes pricing model to a lattice model to estimate fair value at grant date for future option grants. The fair value of each option is estimated on the date of grant or subsequent reload using the lattice pricing model with the following assumptions:

	2006	2005
Weighted average fair value per option	$ 5.98	$ 6.18
Average risk-free interest rate	4.43-4.42%	2.65-4.20%
Expected dividend yield	2.0%	1.8%
Expected volatility	27-32%	27-35%
Expected annual forfeiture rate	3%	—
Expected exercise behavior	23%	32%
Expected life (years)	3.6	3.8

The range of risk-free interest rates is based on a yield curve of interest rates at the time of the grant based on the contractual life of the option. Expected dividend yield is based on a five-year average. Expected volatility is based on historical and implied volatilities over the term of the option. Alcoa utilizes historical option exercise and forfeiture data to estimate expected annual pre- and post-vesting forfeitures. The expected exercise behavior assumption represents a weighted average exercise ratio of gains resulting from historical employee exercise behavior. The 2006 expected exercise behavior assumption is based on exercise patterns for grants issued from 2000 forward.

The activity for stock options is as follows: (shares and aggregate intrinsic value in millions)

	2006
Outstanding at January 1, 2006:	
Number of options	88.6
Weighted average exercise price	$33.50
Granted:	
Number of options	3.1
Weighted average exercise price	$29.13
Exercised:	
Number of options	(5.8)
Weighted average exercise price	$24.26
Expired or forfeited:	
Number of options	(3.9)
Weighted average exercise price	$36.56
Outstanding at June 30, 2006:	
Number of options	82.0
Weighted average exercise price	$33.84
Aggregate intrinsic value	$ 167
Exercisable at June 30, 2006:	
Number of options	78.8
Weighted average exercise price	$34.03
Aggregate intrinsic value	$ 156

The total intrinsic value of options exercised for the second quarter and six-month period ended June 30, 2006, was $37 and $53, respectively. For the second quarter and six-month period ended June 30, 2006, the cash received from exercises was $90 and $136, respectively, and the tax benefit realized was $10 and $15, respectively.

The following tables summarize certain stock option information at June 30, 2006: (shares in millions)

Options Fully Vested and/or Expected to Vest

Range of Exercise price	Number	Weighted average contractual life	Weighted average exercise price	Intrinsic value
$ 4.38 - $12.15	0.1	0.94	$ 11.51	$ 3
$12.16 - $19.93	1.2	1.37	17.09	18
$19.94 - $27.71	9.9	5.31	22.29	101
$27.72 - $35.49	23.7	3.85	30.82	45
$35.50 - $45.59	47.1	3.57	38.28	—
Total	82.0	3.83	33.84	$ 167

Options Fully Vested and Exercisable

Range of Exercise price	Number	Weighted average contractual life	Weighted average exercise price	Intrinsic Value
$ 4.38 - $12.15	0.1	0.94	$ 11.51	$ 3
$12.16 - $19.93	1.2	1.37	17.09	18
$19.94 - $27.71	9.9	5.31	22.27	100
$27.72 - $35.49	20.6	3.61	31.07	35
$35.50 - $45.59	47.0	3.57	38.28	—
Total	78.8	3.76	34.03	$ 156

The following table summarizes the non-vested stock and performance options at June 30, 2006: (shares in millions)

Non-Vested Option Grants

	Number	Weighted average per option FMV
Non-vested at January 1, 2006	4.2	$ 5.51
Granted	3.1	5.98
Vested	(4.0)	5.48
Forfeited	(0.1)	5.77
Non-vested at June 30, 2006	3.2	5.99

The following table summarizes the non-vested stock and performance share awards at June 30, 2006: (shares in millions)

Non-Vested Awards

	Stock Awards	Performance Share Awards	Total	Weighted average FMV
Outstanding at January 1, 2006	2.1	0.5	2.6	$ 31.66
Granted	2.1	0.4	2.5	28.94
Forfeited	(0.2)	—	(0.2)	30.51
Performance share adjustment	—	(0.2)	(0.2)	29.54
Outstanding at June 30, 2006	4.0	0.7	4.7	30.38

For the six-month period ended June 30, 2006, there was $12 (pre-tax) of unrecognized compensation expense related to non-vested stock option grants, and $62 (pre-tax) of unrecognized compensation expense related to stock award grants. These expenses are expected to be recognized over a weighted average period of 2.2 years. As of June 30, 2006, the following table summarizes the unrecognized compensation expense expected to be recognized in future periods.

	Stock-based compensation expense (pre-tax)
Remainder of 2006	$ 20
2007	33
2008	21
Total	$ 74

Alcoa issues treasury shares for the exercise of employee stock options. As of June 30, 2006, 127 million shares of common stock were reserved for issuance under Alcoa's stock-based compensation plans. Alcoa has a policy of repurchasing shares to cover the dilution associated with option exercises and expects to repurchase shares in an amount that approximates options exercised during 2006.

C. Recently Issued and Recently Adopted Accounting Standards – In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109." FIN 48 prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that it has taken or expects to take on a tax return. FIN 48 is effective in the first quarter of 2007. Alcoa is currently evaluating the impact of this statement on the company.

Effective January 1, 2006, Alcoa adopted Emerging Issues Task Force (EITF) Issue No. 04-6, "Accounting for Stripping Costs Incurred During Production in the Mining Industry." EITF 04-6 requires that stripping costs incurred during the production phase of a mine are to be accounted for as variable production costs that should be included in the costs of the inventory produced (that is, extracted) during the period that the stripping costs are incurred. Upon adoption, Alcoa recognized a cumulative effect adjustment in the opening balance of retained earnings of $3, representing the reduction in the net book value of post-production stripping costs of $8, offset by a related deferred tax liability of $3 and minority interests of $2.

D. Restructuring and Other Charges – Alcoa recorded income of $9 ($6 after tax and minority interests) in the 2006 second quarter for restructuring and other charges, resulting from adjustments to prior year severance and other exit cost reserves due to changes in facts and circumstances. In the first quarter of 2006, Alcoa recorded a net charge of $1 ($1 after tax and minority interests) for restructurings associated with previously approved restructuring programs.

For the full year 2005, Alcoa recorded charges of $292 ($190 after tax and minority interests) for restructuring and other items, resulting from the global realignment of Alcoa's organization structure. The 2005 charges were comprised of the following components: $238 of charges for employee termination and severance costs associated with approximately 8,450 salaried and hourly employees, spread globally across the company; $86 related to asset impairments for structures, machinery, and equipment; and $16 for exit costs, consisting primarily of accelerated depreciation associated with assets for which the useful life has been changed due to plans to close certain facilities in the near term. Reversals of previously recorded layoff and other costs of $48 were primarily due to Alcoa's decision to sell certain locations that it previously planned to shut down in 2005. The 2005 restructuring charges have been reclassified from amounts previously reported to reflect the movement of the home exteriors business and the Hawesville, KY automotive casting facility to discontinued operations in 2006. Charges related to these businesses consisted of asset impairments of $45 and a charge of $2 for employee termination and severance costs associated with 183 people. As of June 30, 2006, approximately 4,950 of the 8,450 employees associated with the 2005 restructuring program had been terminated. Cash payments of approximately $21 were made against these reserves in the first half of 2006. The remaining reserves are expected to be paid in cash over the next eighteen months, with the exception of approximately $20 in reserves for ongoing site remediation work over the next several years. Restructuring and other charges are not included in the segment results.

Activity and reserve balances for restructuring charges are as follows:

	Employee termination and severance costs	Other exit costs	Total
Reserve balances at December 31, 2004	$ 24	$ 39	$ 63
2005:			
Cash payments	(78)	(7)	(85)
2005 restructuring charges	238	6	244
Reversals of previously recorded restructuring charges	(48)	—	(48)
Reserve balances at December 31, 2005	136	38	174
2006:			
Cash payments	(21)	—	(21)
2006 restructuring charges	1	3	4
Reversals of previously recorded restructuring charges	(12)	(4)	(16)
Reserve balances at June 30, 2006	$ 104	$ 37	$141

For further details on the 2005 restructurings, see Note D to the audited financial statements contained in the Annual Report on Form 10-K for the year ended December 31, 2005.

E. Pension Plans and Other Postretirement Benefits – The components of net periodic benefit cost follow.

	Second quarter ended June 30		Six months ended June 30	
Pension benefits	**2006**	**2005**	**2006**	**2005**
Service cost	$ 52	$ 52	$ 104	$ 104
Interest cost	155	154	309	308
Expected return on plan assets	(184)	(177)	(369)	(354)
Amortization of prior service cost	3	6	6	12
Recognized actuarial loss	31	23	63	46
Net periodic benefit cost	$ 57	$ 58	$ 113	$ 116

Postretirement benefits	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Service cost	$ 8	$ 8	$ 16	$ 16
Interest cost	51	54	101	108
Expected return on plan assets	(4)	(4)	(8)	(8)
Amortization of prior service cost	2	1	4	2
Recognized actuarial loss	27	15	40	30
Net periodic benefit cost	$ 84	$ 74	$ 153	$ 148

The net periodic benefit cost for postretirement benefits for the second quarter of 2006 and 2005 reflects a reduction of approximately $13 and $6, respectively, related to the recognition of the federal subsidy under Medicare Part D. The net periodic benefit cost for postretirement benefits for the first six months of 2006 and 2005 reflects a reduction of approximately $26 and $12, respectively, related to the Medicare Part D subsidy. For further details on the Medicare Part D subsidy, see Note W to the audited financial statements contained in the Annual Report on Form 10-K for the year ended December 31, 2005.

The four-year labor agreement between Alcoa and the United Steelworkers that was ratified on June 22, 2006 required a remeasurement of certain pension and postretirement benefit plan liabilities due to plan amendments. The discount rate was updated from the December 31, 2005 rate of 5.7% to 6.5% at May 31, 2006. The remeasurement resulted in a decrease in the pension and postretirement benefit obligations of $276 and $76, respectively. The decrease in the liabilities reduces the plans' unrecognized net actuarial losses. To the extent the unrecognized net actuarial losses exceed certain thresholds, the excess will continue to be recognized as prescribed under SFAS No. 87 and SFAS No. 106. Generally, these amounts are amortized over the estimated future service of plan participants. The 2006 net periodic benefit cost increases approximately $4 for pension and $23 for postretirement plans, $15 of which was included in the second quarter of 2006. Other comprehensive income (see Note L) included $94 due to the reduction in the minimum pension liability, primarily resulting from the remeasurement of the plan liability.

F. Other Income, Net

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Equity income (loss)	$ 27	$ (56)	$ 46	$ (21)
Interest income	15	14	32	25
Dividend income	24	19	24	19
Foreign exchange (losses) gains	(19)	5	(17)	—
Gain on sales of assets	7	342	8	342
Other income	7	23	3	18
	$ 61	$ 347	$ 96	$ 383

G. Income Taxes – The effective tax rate of 28.1% for the 2006 six-month period differs from the U.S. federal statutory rate of 35% due to income being taxed in lower rate jurisdictions. It also differs from the 2005 six-month period effective tax rate of 22.2% due to the $120 tax benefit resulting from the finalization of certain tax reviews and audits during the second quarter of 2005. This 2005 benefit was partially offset by a $43 income tax impact of previously undistributed equity earnings related to Alcoa's stake in Elkem ASA which was recorded in the first quarter of 2005.

H. Discontinued Operations and Assets Held for Sale – In the third quarter of 2006, Alcoa reclassified its home exteriors business to discontinued operations upon the signing of a definitive sale agreement with Ply Gem Industries, Inc. In the first quarter of 2006, Alcoa reclassified the Hawesville, KY automotive casting facility to discontinued operations upon closure of the facility. The condensed consolidated financial statements for all periods presented have been reclassified to reflect these businesses in discontinued operations. The operating results of the home exteriors business and the automotive casting facility are not included in the Extruded and End Products segment and the Engineered Solutions segment, respectively.

For the periods presented in the Condensed Consolidated Financial Statements, businesses classified as assets held for sale/discontinued operations included the home exteriors business, the telecommunications business, a small casting facility in Europe, and the Hawesville, KY automotive casting facility. The imaging and graphic communications business, the protective packaging business, and the flexible packaging business in South America were also included in the 2005 discontinued operations results.

In the second quarter of 2006, Alcoa recorded a loss of $5 (after tax and minority interests) from discontinued operations, consisting primarily of operating losses principally related to the casting facility in Europe that was permanently shutdown in the second quarter of 2006. In the first quarter of 2006, Alcoa recorded a loss of $6 (after tax and minority interests) from discontinued operations, consisting of operating losses of $3 and a loss of $3 related to the 2005 sale of the imaging and graphic communications business.

In the second quarter of 2005, Alcoa recorded a loss of $30 (after tax and minority interests) in discontinued operations, consisting of the following: a $28 loss associated with the closure of the Hawesville, KY automotive casting facility, primarily related to asset impairments; $7 in net operating income on businesses to be divested; a $5 loss associated with the divestiture of Alcoa's interest in the AFL telecommunications business; and a $4 impairment charge to reflect the estimated fair value of the protective packaging business. In the first quarter of 2005, Alcoa recorded a loss of $9 (after tax and minority interests) in discontinued operations consisting of the following: a loss of $8 in connection with the divestiture of Alcoa's interest in the AFL telecommunications business; a $4 impairment charge to reflect the estimated fair value of the protective packaging business and the casting facility in Europe; and net operating income of $3.

The following table details selected financial information for the businesses included within discontinued operations.

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Sales	$ 170	$ 258	$ 317	$ 561
(Loss) income from operations, excluding gain (loss) on sale of businesses and loss from impairment	(5)	13	(9)	18
Gain (loss) on sale of businesses	2	—	(2)	(7)
Loss from impairment	(1)	(53)	(1)	(57)
Total pretax loss	(4)	(40)	(12)	(46)
Income tax (expense) benefit	(1)	10	1	4
Minority interests	—	—	—	3
Loss from discontinued operations	$ (5)	$ (30)	$ (11)	$ (39)

The major classes of assets and liabilities of operations held for sale in the balance sheet are as follows:

	June 30, 2006	December 31, 2005
Assets:		
Receivables	$ 106	$ 78
Inventories	45	61
Properties, plants, and equipment, net	57	63
Goodwill	37	37
Other assets	6	9
Total assets held for sale	$ 251	$ 248
Liabilities:		
Accounts payable, accrued expenses, and other	$ 129	$ 126
Total liabilities of operations held for sale	$ 129	$ 126

I. Earnings Per Share – The information used to compute basic and diluted EPS on income from continuing operations follows: (shares in millions)

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Income from continuing operations	$ 749	$ 490	$ 1,363	$ 759
Less: preferred stock dividends	1	1	1	1
Income from continuing operations available to common shareholders	$ 748	$ 489	$ 1,362	$ 758
Average shares outstanding – basic	870	872	870	872
Effect of dilutive securities:				
Shares issuable upon exercise of dilutive stock options	7	6	7	6
Average shares outstanding – diluted	877	878	877	878

Options to purchase 51 million and 73 million shares of common stock at average exercise prices of $38.00 and $36.00 were outstanding as of June 30, 2006 and 2005, respectively, but were not included in the computation of diluted EPS because they were anti-dilutive, as the option exercise price was greater than the average market price of the common shares.

J. Inventories

	June 30, 2006	December 31, 2005
Finished goods	$1,284	$ 962
Work in process	1,282	1,024
Bauxite and alumina	501	486
Purchased raw materials	726	691
Operating supplies	249	229
	$4,042	$ 3,392

Approximately 47% of total inventories at June 30, 2006, was valued on a LIFO basis. If valued on an average cost basis, total inventories would have been $989 and $858 higher at June 30, 2006, and December 31, 2005, respectively. The increase in the LIFO reserve resulted in a charge to cost of goods sold of $75 ($49 after tax) and $131 ($85 after tax) in the second quarter and six-month period ended June 30, 2006.

K. Commitments and Contingencies - Various lawsuits, claims and proceedings have been or may be instituted or asserted against Alcoa, including those pertaining to environmental, product liability, and safety and health matters. While the amounts claimed may be substantial, the ultimate liability cannot now be determined because of the considerable uncertainties that exist. Therefore, it is possible that results of operations or liquidity in a particular period could be materially affected by certain contingencies. However, based on facts currently available, management believes that the disposition of matters that are pending or asserted will not have a materially adverse effect on the financial position or liquidity of the company.

Alcoa Aluminio S.A. (Aluminio) is a participant in several hydroelectric power construction projects in Brazil for purposes of increasing its energy self-sufficiency and providing a long-term, low-cost source of power for its facilities. The Machadinho and Barra Grande projects have been completed. Aluminio's investment participation in these projects is 27.23% for Machadinho and 42.20% for Barra Grande.

Aluminio committed to taking a share of the output of the Machadinho project, completed in 2002, for 30 years at cost (including cost of financing the project). In the event that other participants in this project fail to fulfill their financial responsibilities, Aluminio may be required to fund a portion of the deficiency. In accordance with the agreement, if Aluminio funds any such deficiency, its participation and share of the output from the project will increase proportionately.

Barra Grande operations started up in November 2005 and full capacity was reached in February 2006. With Machadinho and Barra Grande, Aluminio's current power self-sufficiency is approximately 38%, to meet a total energy demand of approximately 690 megawatts from Brazilian primary plants. Aluminio accounts for the Machadinho and Barra Grande hydroelectric projects on the equity method. Its total investment in these projects was $165 and $152 at June 30, 2006 and December 31, 2005, respectively. Alcoa's maximum exposure to loss on these completed projects is $491, which represents Alcoa's investment and guarantees of debt.

In the first quarter of 2006, Aluminio acquired an additional 6.41% share in the Estreito hydroelectric power project, reaching 25.49% of total participation in the consortium. This additional share entitles Aluminio to 38 megawatts of assured energy. The project will have total installed capacity of 1,087 megawatts and assured power of 589 megawatts. In September 2005, the consortium submitted the necessary plans to obtain the environmental installation license. Upon completion of certain socioeconomic and cultural impact studies as required by a governmental agency, construction is expected to begin in the fourth quarter of 2006.

In 2004, Alcoa agreed to acquire a 20% interest in a consortium formed to acquire the Dampier to Bunbury Natural Gas Pipeline (DBNGP) in Western Australia in exchange for an initial cash investment of $17, which was classified as an equity investment. Alcoa has made additional contributions of $36, including $12 in the second quarter of 2006 and $5 in the first quarter of 2006, and committed to invest an additional $39 to be paid as the pipeline expands through 2007. The investment in the DBNGP was made in order to secure a competitively priced long-term supply of power to Alcoa's refineries in Western Australia. In addition to its equity ownership, Alcoa has an agreement to purchase gas transmission services from the DBNGP. Alcoa's maximum exposure to loss on the investment and the related contract is approximately $300.

On July 20, 2006, the European Commission (EC) announced that it has opened an investigation to establish whether an extension of the regulated preferential electricity tariff granted by Italy to some energy intensive industries complies with EC Treaty state aid rules. The new Italian power tariff modifies the preferential tariff that was in force until December 31, 2005 and extends it through 2010. Alcoa has been operating in Italy for more than 10 years under a power supply structure approved by the EU Commission in 1996. That measure, like the new one, was based on Italian state legislation that provides a competitive power supply to the primary aluminum industry and is not considered state aid by the Italian Government. The Commission's announcement states that it has doubts about the measure's compatibility with EU legislation and concerns about distortion of competition in the European market of primary aluminum, where energy is an important part of the production costs. The opening of an in-depth investigation gives interested parties the opportunity to comment on the proposed measures. It does not prejudge the outcome of the procedure. It is Alcoa's understanding that the Italian Government's continuation of the electricity tariff was done in conformity with all applicable laws and regulations. Alcoa believes that the total potential impact from a loss of the tariff would be approximately $17 (pre-tax) per month in higher power costs at its Italian smelters.

L. Comprehensive Income

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Net income	$ 744	$ 460	$1,352	$ 720
Changes in other comprehensive income, net of tax:				
Unrealized losses on available-for-sale securities	(181)	(13)	(12)	(21)
Unrealized translation adjustments	169	(361)	203	(448)
Change in minimum pension liability	94	—	94	—
Unrecognized (losses) gains on derivatives:				
Net change from periodic revaluations	(164)	28	(305)	87
Net amount reclassified to income	(18)	(24)	(53)	(40)
Net unrecognized (losses) gains on derivatives	(182)	4	(358)	47
Comprehensive income	$ 644	$ 90	$1,279	$ 298

M. Segment Information – Alcoa's reportable segments, as reclassified for discontinued operations and assets held for sale, follow. The differences between segment totals and consolidated totals are in Corporate.

	Alumina	Primary Metals	Flat-Rolled Products	Extruded and End Products	Engineered Solutions	Packaging and Consumer	Total
Second quarter ended June 30, 2006							
Sales:							
Third-party sales	$ 713	$1,589	$ 2,115	$ 1,165	$ 1,405	$ 834	$ 7,821
Intersegment sales	515	1,696	66	31	—	—	2,308
Total sales	$1,228	$3,285	$ 2,181	$ 1,196	$ 1,405	$ 834	$10,129
Profit and loss:							
Equity income (loss)	$ —	$ 28	$ (1)	$ —	$ —	$ —	$ 27
Depreciation, depletion and amortization	46	102	57	30	42	31	308
Income taxes	112	209	25	8	44	9	407
ATOI	278	489	79	17	100	37	1,000
Second quarter ended June 30, 2005							
Sales:							
Third-party sales	$ 533	$1,124	$ 1,763	$ 992	$ 1,282	$ 827	$ 6,521
Intersegment sales	439	1,215	36	19	–	–	1,709
Total sales	$ 972	$2,339	$ 1,799	$ 1,011	$ 1,282	$ 827	$ 8,230
Profit and loss:							
Equity loss	$ —	$ (76)	$ —	$ —	$ —	$ —	$ (76)
Depreciation, depletion and amortization	43	90	54	30	45	31	293
Income taxes	66	75	27	13	30	18	229
ATOI	182	187	70	14	61	41	555

	Alumina	Primary Metals	Flat-Rolled Products	Extruded and End Products	Engineered Solutions	Packaging and Consumer	Total
Six months ended June 30, 2006							
Sales:							
Third-party sales	$1,341	$2,997	$4,055	$2,203	$2,765	$1,583	$14,944
Intersegment sales	1,070	3,217	115	54	—	—	4,456
Total sales	$2,411	$6,214	$4,170	$2,257	$2,765	$1,583	$19,400
Profit and loss:							
Equity (loss) income	$(1)	$48	$(1)	$—	$—	$—	$46
Depreciation, depletion and amortization	89	198	107	58	82	62	596
Income taxes	205	406	51	9	81	14	766
ATOI	520	934	145	17	183	45	1,844
Six months ended June 30, 2005							
Sales:							
Third-party sales	$1,038	$2,213	$3,418	$1,907	$2,519	$1,535	$12,630
Intersegment sales	832	2,518	70	33	—	—	3,453
Total sales	$1,870	$4,731	$3,488	$1,940	$2,519	$1,535	$16,083
Profit and loss:							
Equity (loss) income	$(1)	$(58)	$—	$—	$1	$1	$(57)
Depreciation, depletion and amortization	84	180	106	59	92	63	584
Income taxes	127	167	51	11	56	28	440
ATOI	343	412	145	25	122	57	1,104

The following reconciles segment information to consolidated totals.

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Total ATOI	$1,000	$555	$1,844	$1,104
Impact of LIFO and intersegment profit adjustments **	13	(18)	37	(20)
Unallocated amounts (net of tax):				
Interest income	10	9	21	16
Interest expense	(63)	(56)	(123)	(107)
Minority interests	(124)	(60)	(229)	(120)
Corporate expense	(82)	(73)	(171)	(142)
Restructuring and other charges	6	(144)	5	(174)
Discontinued operations	(5)	(30)	(11)	(39)
Other **	(11)	277	(21)	202
Consolidated net income	$744	$460	$1,352	$720

** Prior periods corporate LIFO expense has been reclassified from “Other” to combine the total impact of inventory related items.

The following table details segment assets.

	June 30, 2006	December 31, 2005
Alumina	$ 4,573	$ 4,268
Primary Metals	9,698	8,566
Flat-Rolled Products	5,069	3,963
Extruded and End Products	2,438	2,021
Engineered Solutions	6,049	5,733
Packaging and Consumer	2,840	2,787
Total segment assets	$30,667	$ 27,338

N. Acquisitions and Divestitures – On June 30, 2006, Alcoa completed the acquisition of the minority interests (including the purchase of certain raw material inventories) in its Intalco and Eastalco aluminum smelters in Ferndale, Washington, and Frederick, Maryland, respectively, in exchange for the assumption of certain liabilities related to the facilities and receipt of a net cash payment of $25.

In April 2006, Alcoa initiated the acquisition of its 70% interest in the aluminum brazing sheet venture in Kunshan City, China. Alcoa will be the managing partner in the venture, with the remaining 30% shares held by Shanxi Yuncheng Engraving Group. The total purchase price is expected to be approximately $61, of which $33 has been paid through June 2006. The transaction is expected to be completed in the third quarter of 2006.

O. Reclassifications - Certain amounts have been reclassified to conform to current period presentation.

Report of Independent Registered Public Accounting Firm*

To the Shareholders and Board of Directors of Alcoa Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Alcoa Inc. and its subsidiaries (Alcoa) as of June 30, 2006, and the related condensed statement of consolidated income for each of the three-month and six-month periods ended June 30, 2006 and 2005 and the condensed statement of consolidated cash flows for the six-month periods ended June 30, 2006 and 2005. These interim financial statements are the responsibility of Alcoa's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2005, and the related statements of consolidated income, of shareholders' equity and of cash flows for the year then ended, management’s assessment of the effectiveness of Alcoa's internal control over financial reporting as of December 31, 2005 and the effectiveness of Alcoa's internal control over financial reporting as of December 31, 2005; and in our report dated February 17, 2006, except with respect to our opinion on the consolidated financial statements insofar as it relates to the effects of the discontinued operations discussed in Note B to those consolidated financial statements, as to which the date is January 15, 2007, we expressed unqualified opinions thereon. The consolidated financial statements and management’s assessment of the effectiveness of internal control over financial reporting referred to above are not presented herein. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2005, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP

Pittsburgh, Pennsylvania
July 26, 2006, except with respect to the effects of the discontinued operations discussed in Note H, as to which the date is January 15, 2007.

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* This report should not be considered a “report” within the meanings of Sections 7 and 11 of the 1933 Act and the independent accountant’s liability under Section 11 does not extend to it.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
(dollars in millions, except per share amounts and ingot prices; shipments in thousands of metric tons [mt])

Certain statements in this report under this caption and elsewhere relate to future events and expectations and, as such, constitute forward-looking statements. Forward-looking statements include those containing such words as "anticipates," "believes," "estimates," "expects," "hopes," "targets," "should," "will," "will likely result," "forecast," "outlook," "projects" or similar expressions. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of Alcoa to be different from those expressed or implied in the forward-looking statements. For a discussion of some of the specific factors that may cause such a difference, see Note K to the Condensed Consolidated Financial Statements; the disclosures included below under Segment Information, Environmental Matters, and Quantitative and Qualitative Disclosures about Market Risks; and Alcoa's Form 10-K, Part I, Item 1A, for the year ended December 31, 2005. Alcoa disclaims any intention or obligation (other than as required by law) to update or revise any forward-looking statements.

Results of Operations

***Selected Financial Data*:**

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Sales	$ 7,797	$ 6,532	$14,908	$12,631
Income from continuing operations	749	490	1,363	759
Loss from discontinued operations	(5)	(30)	(11)	(39)
Net income	744	460	1,352	720
Earnings per common share:				
Diluted – Income from continuing operations	$ .85	$ .56	$ 1.55	$ .86
Diluted – Net income	.85	.52	1.54	.82
Shipments of aluminum products (mt)	1,400	1,389	2,750	2,668
Shipments of alumina (mt)	2,108	1,951	4,131	3,874
Alcoa's average realized ingot price per metric ton	$ 2,728	$ 1,977	$ 2,633	$ 2,010
Average 3-month LME price per metric ton	2,681	1,797	2,562	1,845

Alcoa's income from continuing operations for the 2006 second quarter and six-month period was $749, or 85 cents per diluted share, and $1,363, or $1.55 per share, respectively. Income from continuing operations increased 53% in the 2006 second quarter and 80% in the 2006 six-month period compared to the corresponding periods in 2005, primarily due to higher realized prices for alumina which rose 33% and 28% in the 2006 second quarter and six-month period, respectively, and higher realized prices for aluminum which rose 38% and 31% in the 2006 second quarter and six-month period, respectively, compared with the corresponding periods of 2005, and higher volumes primarily in the Alumina, Flat-Rolled Products, Engineered Solutions, and Extruded and End Products segments. The absence in 2006 of restructuring charges for layoffs and asset impairments recognized in the 2005 second quarter and six-month period also favorably impacted results in 2006. The 2006 results were negatively impacted by higher raw material, energy and other input costs, labor contract and strike preparation costs, the absence of the $180 net gain recognized on the sale of Alcoa's stake in Elkem ASA which occurred in the 2005 second quarter, and the absence of a tax benefit of $120 related to the finalization of certain tax reviews and audits in the 2005 second quarter.

Net income for the 2006 second quarter and six-month period was $744, or 85 cents per share, and $1,352, or $1.54 per share, respectively, compared with $460, or 52 cents per share, and $720, or 82 cents per share, for the corresponding periods of 2005. Net income in 2006 included losses from discontinued operations of $5 and $11 in the second quarter and six-month period, respectively, consisting primarily of operating losses, as well as $5 for the shutdown of the casting facility in Europe in the 2006 second quarter, and a loss of $3 related to the 2005 sale of the imaging and graphic communications business in the 2006 first quarter. Net income in 2005 included losses from discontinued operations of $30 and $39 in the second quarter and six-month period, respectively, consisting primarily of a $28 loss for asset impairments associated with the closure of the Hawesville, KY automotive casting facility.

Sales for the second quarter and six-month period of 2006 increased $1,265, or 19%, and $2,277, or 18%, compared with the 2005 corresponding periods. The increase in sales was driven by higher realized prices for alumina and aluminum; strong demand in businesses serving the aerospace, building and construction, commercial transportation, packaging (can sheet), and distribution markets; higher volumes in four of six segments; and increased sales related to metal purchased and subsequently resold. Partially offsetting these increases were unfavorable foreign currency exchange movements and the impact of the Eastalco smelter curtailment.

Cost of goods sold (COGS) as a percentage of sales was 74.7% in the second quarter of 2006 compared with 80.8% in the second quarter of 2005, and 74.9% in the 2006 six-month period compared with 80.0% in the corresponding 2005 period. Higher realized prices and higher volumes, which were somewhat offset by higher energy, raw material and other input costs, as well as labor contract and strike preparation costs, contributed to the percentage improvement.

Selling, general administrative, and other expenses (SG&A) increased $21 in the second quarter of 2006 and $66 in the 2006 six-month period compared with the corresponding periods of 2005. The increase in both periods principally resulted from higher expense associated with stock-based compensation, as well as increased deferred compensation costs in 2006. SG&A as a percentage of sales decreased from 5.1% in the 2005 second quarter to 4.5% in the second quarter of 2006 and from 5.1% in the 2005 six-month period to 4.8% in the 2006 six-month period.

Restructuring and other charges consisted of income of $9 ($6 after tax and minority interests) in the 2006 second quarter and $8 ($5 after tax and minority interests) in the 2006 six-month period, primarily resulting from adjustments to prior year severance and other exit cost reserves due to changes in facts and circumstances. Restructuring and other charges were $214 ($142 after tax and minority interests) in the 2005 second quarter and $259 ($167 after tax and minority interests) in the 2005 six-month period, resulting from the global realignment of Alcoa's organization structure. The charges for the first half of 2005 were comprised of $192 for employee termination and severance costs, $63 for asset impairments, and $4 for other exit costs.

As of June 30, 2006, approximately 4,950 of the 8,450 employees associated with the 2005 restructuring program had been terminated and cash payments of $21 were made against the reserves in the first half of 2006. The remaining reserves are expected to be paid in cash over the next eighteen months, with the exception of approximately $20 in reserves for ongoing site remediation work over the next several years.

Restructuring and other charges are not included in the segment results. The pre-tax impact of allocating these amounts to the segment results would have been as follows:

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Alumina	$ —	$ (2)	$ —	$ (4)
Primary Metals	2	(19)	—	(21)
Flat-Rolled Products	5	(7)	5	(11)
Extruded and End Products	—	(64)	(2)	(71)
Engineered Solutions	1	(80)	2	(97)
Packaging and Consumer	—	(25)	2	(37)
Segment total	8	(197)	7	(241)
Corporate	1	(17)	1	(18)
Total restructuring and other charges	$ 9	$ (214)	$ 8	$ (259)

Interest expense for the 2006 second quarter and six-month period increased $11, or 13%, and $25, or 15%, compared with the corresponding periods in 2005, primarily due to higher average debt levels and higher effective interest rates.

Other income declined $286, or 82%, in the second quarter of 2006, and $287, or 75%, in the six-month period of 2006, compared with the corresponding periods of 2005. The decrease in both periods is primarily due to the $345 gain recognized on the sale of Alcoa's stake in Elkem ASA in 2005, as well as unfavorable foreign currency exchange movements, partially offset by an increase in equity income due to the absence of the $90 charge recognized in 2005 for impairment, layoff and other costs related to the closure of the Hamburger Aluminium-Werk facility in Germany.

The effective tax rate of 28.1% for the 2006 six-month period differs from the U.S. federal statutory rate of 35% due to income being taxed in lower rate jurisdictions. It also differs from the 2005 six-month period effective tax rate of 22.2% due to the $120 tax benefit resulting from the finalization of certain tax reviews and audits during the second quarter of 2005. This benefit was partially offset by a $43 income tax impact of previously undistributed equity earnings related to Alcoa's stake in Elkem ASA which was recorded in the first quarter of 2005.

Minority interests' share of income from operations increased $64, or 107%, and $109, or 91%, in the 2006 second quarter and six-month period, respectively, compared with the 2005 corresponding periods. The increase was principally due to higher earnings at Alcoa World Alumina and Chemicals (AWAC), as an increase in realized prices and higher volumes contributed to the increase in earnings.

On June 22, 2006, a new four-year agreement was ratified between Alcoa and the United Steelworkers (USW) that covers approximately 9,000 U.S. employees across 15 locations. The new master agreement contract includes structural changes in employee and retiree health care programs, resulting in additional employee cost sharing through plan design changes and premium contributions. The contract also contains provisions for a signing bonus upon ratification, wage increases and pension factor increases for longer service employees. The impact on Alcoa's results of operations associated with the provisions in the new contract, as well as costs incurred in preparation for a potential work stoppage was a pre-tax charge of approximately $50 in the second quarter of 2006.

Segment Information

I. Alumina

	Second quarter ended June 30		Six months ended June 30	
	2006	**2005**	**2006**	**2005**
Alumina production (mt)	3,746	3,621	7,448	7,204
Third-party alumina shipments (mt)	2,108	1,951	4,131	3,874
Third-party sales	$ 713	$ 533	$1,341	$1,038
Intersegment sales	515	439	1,070	832
Total sales	$ 1,228	$ 972	$2,411	$1,870
After-tax operating income (ATOI)	$ 278	$ 182	$ 520	$ 343

Third-party sales for the Alumina segment increased 34% in the 2006 second quarter and 29% in the 2006 six-month period, compared with the corresponding 2005 periods, primarily due to an increase in realized prices of 33% in the second quarter of 2006 and 28% in the 2006 six-month period, compared with the corresponding 2005 periods. Additionally, third-party volumes increased 8% and 7% in the 2006 second quarter and six-month period, respectively. Intersegment sales increased 17% and 29% in the 2006 second quarter and six-month period, respectively, compared with the corresponding periods of 2005, as a result of higher realized prices.

ATOI for this segment increased 53% and 52% in the 2006 second quarter and six-month period, respectively, compared with the corresponding 2005 periods, due to higher LME-based prices and higher volumes, somewhat offset by increased costs for raw materials and energy.

During the third quarter of 2006, the Alumina segment is expected to benefit from anticipated productivity gains. Production volume is also expected to increase as a result of the ongoing ramp-up of the recently completed Pinjarra expansion.

II. Primary Metals

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Aluminum production (mt)	882	899	1,749	1,750
Third-party aluminum shipments (mt)	508	520	996	1,007
Alcoa's average realized price for aluminum ingot (per mt)	$ 2,728	$ 1,977	$2,633	$2,010
Third-party sales	$ 1,589	$ 1,124	$2,997	$2,213
Intersegment sales	1,696	1,215	3,217	2,518
Total sales	$ 3,285	$ 2,339	$6,214	$4,731
After-tax operating income (ATOI)	$ 489	$ 187	$ 934	$ 412

Third-party sales for the Primary Metals segment increased 41% in the 2006 second quarter and 35% in the 2006 six-month period, compared with the corresponding 2005 periods, primarily due to an increase in realized prices of 38% in the second quarter of 2006 and 31% in the 2006 six-month period, compared with the corresponding 2005 periods. Third-party shipments decreased by 2% in the second quarter of 2006 compared to the corresponding 2005 period due mainly to the 2% decline in production for the same period as a result of the temporary curtailment of the Eastalco, MD smelter in December 2005, partially offset by the Alumar, Brazil smelter expansion substantially completed in March 2006. Intersegment sales increased 40% and 28% in the 2006 second quarter and six-month period, respectively, compared with the corresponding periods of 2005, primarily due to higher realized prices.

ATOI for this segment increased 162% and 127% in the 2006 second quarter and six-month period, respectively, compared with the corresponding 2005 periods, due to higher LME and realized prices, partially offset by higher energy, raw material, and strike preparation and related costs associated with the renegotiation of the USW master agreement contract, and unfavorable foreign currency exchange movements associated with the Brazilian Real and Canadian dollar, somewhat offset by the Euro.

Alcoa has approximately 621,000 metric tons per year (mtpy) of idle capacity on a base capacity of 4,251,000 mtpy. Base capacity increased by 62,000 mtpy in the first quarter of 2006 due to the completion of the Alumar expansion and by 185,000 mtpy in the second quarter of 2006 with the acquisition of the minority interests in its Intalco, WA and Eastalco, MD smelters.

In the third quarter, production will improve due to the continued return to service of the Portland smelter. Production is not expected to reach full capacity at the Portland smelter until January 2007. Based on this segment's LME-linked supply contracts, alumina and power costs will increase in the third quarter. This segment realizes metal prices on an approximate 30-day lag and, as a result, may be exposed to lower LME prices in the third quarter as the LME declined in June 2006 compared to the second quarter.

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III. Flat-Rolled Products

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Third-party aluminum shipments (mt)	579	560	1,141	1,069
Third-party sales	$ 2,115	$ 1,763	$4,055	$3,418
Intersegment sales	66	36	115	70
Total sales	$ 2,181	$ 1,799	$4,170	$3,488
After-tax operating income (ATOI)	$ 79	$ 70	$ 145	$ 145

Third-party sales for the Flat-Rolled Products segment increased 20% in the 2006 second quarter and 19% in the 2006 six-month period, compared with the corresponding 2005 periods, primarily due to strong volume and mix within the aerospace and can sheet markets.

ATOI for this segment increased 13% in the 2006 second quarter and was flat in the 2006 six-month period compared with the corresponding 2005 periods. The increase in ATOI in the 2006 second quarter was due to strong aerospace and can sheet volumes and mix, which more than offset the impact of higher energy and raw material costs and labor contract and strike preparation costs. ATOI was flat in the 2006 six-month period, as stronger volumes and mix were entirely offset by the higher costs noted previously.

In the third quarter, demand is expected to remain strong in the aerospace and can sheet markets. Typical seasonal decreases are anticipated in the automotive market and European markets due to seasonal customer shutdowns and maintenance activities, while energy costs are anticipated to rise toward the end of the summer months.

IV. Extruded and End Products

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Third-party aluminum shipments (mt)	231	226	454	437
Third-party sales	$ 1,165	$ 992	$ 2,203	$1,907
Intersegment sales	31	19	54	33
Total sales	$ 1,196	$ 1,011	$2, 257	$1,940
After-tax operating income (ATOI)	$ 17	$ 14	$ 17	$ 25

Third-party sales for the Extruded and End Products segment increased 17% in the 2006 second quarter and 16% in the 2006 six-month period, compared with the corresponding 2005 periods, primarily due to stronger volumes in commercial transportation, building and construction, and distribution across all businesses.

ATOI for this segment increased 21% in the 2006 second quarter compared with the 2005 second quarter. The increase in the 2006 second quarter was primarily due to volume gains partially offset by higher energy and other input cost inflation. ATOI declined 32% in the 2006 six-month period compared with the corresponding period of 2005. The decline in the 2006 six-month period was due to operating losses at the Russian facilities and higher raw material and energy costs.

In the third quarter, consistent market and operational conditions in line with the second quarter are anticipated.

V. Engineered Solutions

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Third-party aluminum shipments (mt)	38	37	75	75
Third-party sales	$ 1,405	$ 1,282	$2,765	$2,519
Intersegment sales	—	—	—	—
Total sales	$ 1,405	$ 1,282	$2,765	$2,519
After-tax operating income (ATOI)	$ 100	$ 61	$ 183	$ 122

Third-party sales for the Engineered Solutions segment increased 10% in both the 2006 second quarter and six-month period, compared with the corresponding 2005 periods primarily due to continued strong demand in the aerospace, commercial transportation, and industrial markets, as well as capturing raw material increases in prices.

ATOI for this segment increased 64% and 50% in the 2006 second quarter and six-month period, respectively, compared with the corresponding 2005 periods, due to strong market demand, improved productivity, mix management efforts, and cost savings resulting from the 2005 restructuring program.

Demand in the aerospace and commercial transportation markets is expected to remain strong through the third quarter of 2006. However, the North American automotive and European markets are anticipated to weaken due to normally scheduled shutdowns.

VI. Packaging and Consumer

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Third-party aluminum shipments (mt)	44	46	84	80
Third-party sales	$ 834	$ 827	$1,583	$1,535
Intersegment sales	—	—	—	—
Total sales	$ 834	$ 827	$1,583	$1,535
After-tax operating income (ATOI)	$ 37	$ 41	$ 45	$ 57

Third-party sales for the Packaging and Consumer segment were relatively flat in the 2006 second quarter and increased 3% in the 2006 six-month period, compared with the corresponding 2005 periods. The increase was primarily due to improved pricing and increased volumes in the consumer products and closures businesses, offset somewhat by weakness in food packaging.

ATOI for this segment declined 10% and 21% in the 2006 second quarter and six-month period, respectively, compared with the corresponding 2005 periods. The decreases were due to higher transportation costs, energy costs, less favorable mix, and pricing challenges in the food packaging business. These negatives were offset somewhat by productivity improvements and the higher year-to-date volumes in the consumer and closures businesses noted above.

In the third quarter, a normal seasonal slowdown in the closures business is anticipated.

Reconciliation of ATOI to Consolidated Net Income

Items required to reconcile ATOI to consolidated net income include: certain effects of LIFO inventory accounting and intersegment profit adjustments; interest income and expense; minority interests; corporate expense, comprised of the general administrative and selling expenses of operating the corporate headquarters and other global administrative facilities along with depreciation and amortization on corporate-owned assets; restructuring and other charges; discontinued operations; and other, which includes the differences between estimated tax rates used in the segments and the corporate effective tax rate, and other nonoperating items such as foreign currency translation gains/losses.

The following reconciles segment information to consolidated totals.

	Second quarter ended June 30		Six months ended June 30	
	2006	2005	2006	2005
Total ATOI	$ 1,000	$ 555	$1,844	$1,104
Impact of LIFO and intersegment profit adjustments *	13	(18)	37	(20)
Unallocated amounts (net of tax):				
Interest income	10	9	21	16
Interest expense	(63)	(56)	(123)	(107)
Minority interests	(124)	(60)	(229)	(120)
Corporate expense	(82)	(73)	(171)	(142)
Restructuring and other charges	6	(144)	5	(174)
Discontinued operations	(5)	(30)	(11)	(39)
Other *	(11)	277	(21)	202
Consolidated net income	$ 744	$ 460	$1,352	$ 720

* Prior periods corporate LIFO expense has been reclassified from "Other" to combine the total impact of inventory related items.

The significant changes in the reconciling items between ATOI and consolidated net income for the 2006 second quarter and six-month period compared with the corresponding 2005 periods consisted of:

- The change in the impact of LIFO and intersegment profit adjustments was attributed to higher input costs in the segments in 2006,
- an increase in minority interests, due to an increase in earnings at Alcoa World Alumina and Chemicals (AWAC),
- an increase in corporate expenses, primarily due to increased stock-based compensation expenses,
- a decrease in restructuring and other charges due to the absence of new restructurings in 2006, and
- a decrease in other, which in the first half of 2005 consisted of the net gain on the sale of Alcoa's stake in Elkem of $180, the $120 tax benefit related to the finalization of certain tax reviews and audits, slightly offset by the $58 charge related to the closure of the Hamburger Aluminium-Werk facility in Germany.

The following table details segment assets.

	June 30, 2006	December 31, 2005
Alumina	$ 4,573	$ 4,268
Primary Metals	9,698	8,566
Flat-Rolled Products	5,069	3,963
Extruded and End Products	2,438	2,021
Engineered Solutions	6,049	5,733
Packaging and Consumer	2,840	2,787
Total segment assets **	$30,667	$ 27,338

** The difference between the segment total and consolidated assets is in Corporate.

The increase in segment assets across all segments in the first half of 2006 was primarily due to higher customer receivables and increased inventories from favorable market conditions, higher realized prices, and the strategic, targeted building of inventory in preparation for a potential work stoppage. The increase in segment assets in the Alumina and Primary Metals segments was also due to capital spending on growth projects, including alumina refinery upgrades in Pinjarra, Australia and Jamaica, as well as the construction of the smelter in Iceland and the anode plant in Norway.

Statement of Financial Position

Comprehensive income was $644 in the second quarter ended June 30, 2006, which consisted primarily of $744 in net income for the second quarter; $181 in unrealized losses on available-for-sale securities; a $169 increase in unrealized translation adjustments due to a weaker U.S. Dollar; a $94 change in the minimum pension liability due to the remeasurement, using an updated discount rate, of certain pension and postretirement benefit plan liabilities due to plan amendments associated with the ratification of the four-year labor agreement between Alcoa and the USW; and unrecognized losses on derivatives of $182, principally due to the decrease in the fair value of aluminum and natural gas cash flow hedges.

Comprehensive income was $1,279 in the six-month period ended June 30, 2006, which consisted primarily of $1,352 in net income; $12 in unrealized losses on available-for-sale securities; a $203 increase in unrealized translation adjustments due to a weaker U.S. Dollar; a $94 change in the minimum pension liability as noted previously; and unrecognized losses on derivatives of $358, due to the decrease in the fair value of aluminum and natural gas cash flow hedges.

Liquidity and Capital Resources

Cash from Operations

Cash from operations was $486 in the 2006 six-month period compared with cash from operations of $145 in the same period of 2005. The increase of $341 is principally due to higher earnings, partially offset by increased working capital requirements.

Financing Activities

Cash provided from financing activities was $540 in the 2006 six-month period, a change of $239 compared with cash from financing activities of $301 in the corresponding period of 2005. The change was principally due to a net increase in borrowings of $402, primarily commercial paper used to fund working capital requirements and capital projects, partially offset by cash used to pay dividends to minority interests and to repurchase common stock to offset the dilutive effect associated with stock option exercises.

Investing Activities

Cash used for investing activities was $1,352 in the 2006 six-month period compared with $437 in the 2005 six-month period. The increase in cash used of $915 was primarily due to: a $487 increase in capital expenditures primarily related to growth projects including the construction of the Iceland smelter, the anode facility in Norway, and alumina refinery upgrades in Pinjarra, Australia and Jamaica; the absence of cash proceeds of $1,077 in 2005 from the sale of Alcoa's stake in Elkem ASA and Integris Metals; and the absence of cash outlays for acquisitions that used $433 in 2005 associated with the two Russian fabricating facilities and the acquisition of full ownership of the AFL automotive business.

Critical Accounting Policies and Estimates

On January 1, 2006, Alcoa adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), "Share-Based Payment," which requires the company to recognize compensation expense for stock-based compensation based on the fair value of the share-based employee grants. SFAS No. 123(R) revises SFAS No. 123 "Accounting for Stock-Based Compensation" and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Alcoa elected the modified prospective application method for adoption, and prior periods financial statements have not been restated.

Alcoa recognizes compensation expense for employee equity grants using the non-substantive vesting period approach, in which the expense (net of estimated forfeitures) is recognized ratably over the requisite service period following the date of grant. Prior to the adoption of SFAS No. 123(R), Alcoa used the nominal vesting approach related to retiree-eligible employees, in which the compensation expense is recognized ratably over the original vesting period. As part of Alcoa's stock-based compensation plan design, individuals that are retirement-eligible have a six-month requisite service period in the year of grant. Equity grants are issued in early January each year. As a result, a larger portion of expense will be recognized in the first and second quarters of each year for these retiree-eligible employees. Compensation expense for the second quarter and six-month period ended June 30, 2006 was $22 ($13 after tax) and $50 ($33 after tax), respectively. Of these amounts, $10 and $30 in the second quarter and six-month period, respectively, pertain to retirement-eligible employees.

As of January 1, 2005, Alcoa switched from the Black-Scholes pricing model to a lattice model to estimate fair value at grant date for future option grants. On December 31, 2005, Alcoa accelerated the vesting of 11 million unvested stock options granted to employees in 2004 and on January 13, 2005. The 2004 and 2005 accelerated options had weighted average exercise prices of $35.60 and $29.54, respectively, and in the aggregate represented approximately 12 percent of Alcoa's total outstanding options. The decision to accelerate the vesting of the 2004 and 2005 options was made primarily to avoid recognizing the related compensation expense in future financial statements upon the adoption of SFAS No. 123(R). Alcoa expects the accelerated vesting of the 2004 and 2005 stock options to reduce its after-tax stock option compensation expense by $21 in 2006 and by $7 in 2007.

An additional change has been made to the stock-based compensation program for 2006 grants. Plan participants can choose whether to receive their award in the form of stock options, restricted stock units (stock awards), or a combination of both. This choice is made before the grant is issued and is irrevocable. This choice resulted in an increased stock award expense in comparison to 2005.

SFAS No. 123(R) requires Alcoa to recognize compensation expense for stock-based compensation ratably over the requisite service period based on the fair value of the grant. Determining the fair value of stock options at grant date requires judgment including estimates for the average risk-free interest rate, expected volatility, expected exercise behavior, expected dividend yield, and expected forfeitures. If any of these assumptions differ significantly from actual, stock-based compensation expense could be impacted. Prior to the adoption of SFAS No. 123(R), the company accounted for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations using the intrinsic value method, which resulted in no compensation cost for options granted.

Recently Issued and Recently Adopted Accounting Standards

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109." FIN 48 prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that it has taken or expects to take on a tax return. FIN 48 is effective in the first quarter of 2007. Alcoa is currently evaluating the impact of this statement on the company.

Effective January 1, 2006, Alcoa adopted Emerging Issues Task Force (EITF) Issue No. 04-6, "Accounting for Stripping Costs Incurred During Production in the Mining Industry." EITF 04-6 requires that stripping costs incurred during the production phase of a mine are to be accounted for as variable production costs that should be included in the costs of the inventory produced (that is, extracted) during the period that the stripping costs are incurred. Upon adoption, Alcoa recognized a cumulative effect adjustment in the opening balance of retained earnings of $3, representing the reduction in the net book value of post-production stripping costs of $8, offset by a related deferred tax liability of $3 and minority interests of $2.

Environmental Matters

Alcoa continues to participate in environmental assessments and cleanups at a number of locations. These include approximately 36 owned or operating facilities and adjoining properties, approximately 34 previously owned or operating facilities and adjoining properties and approximately 66 waste sites, including Superfund sites. A liability is recorded for environmental remediation costs or damages when a cleanup program becomes probable and the costs or damages can be reasonably estimated.

As assessments and cleanups proceed, the liability is adjusted based on progress made in determining the extent of remedial actions and related costs and damages. The liability can change substantially due to factors such as the nature and extent of contamination, changes in remedial requirements, and technological changes. Therefore, it is not possible to determine the outcomes or to estimate with any degree of accuracy the potential costs for certain of these matters.

The following discussion provides additional details regarding the current status of Alcoa's significant sites where the final outcome cannot be determined or the potential costs in the future cannot be estimated.

Massena, NY. Alcoa has been conducting investigations and studies of the Grasse River, adjacent to Alcoa's Massena, New York plant site, under order from the U.S. Environmental Protection Agency

(EPA) issued under the Comprehensive Environmental Response, Compensation and Liability Act, also known as Superfund. Sediments and fish in the river contain varying levels of polychlorinated biphenyl (PCB).

In 2002, Alcoa submitted an Analysis of Alternatives Report that detailed a variety of remedial alternatives with estimated costs ranging from $2 to $525. Because the selection of the $2 alternative (natural recovery) was considered remote, Alcoa adjusted the reserve for the Grasse River in 2002 to $30 representing the low end of the range of possible alternatives, as no single alternative could be identified as more probable than the others.

In June of 2003, based on river observations during the spring of 2003, the EPA requested that Alcoa gather additional field data to assess the potential for sediment erosion from winter river ice formation and breakup. The results of these additional studies, submitted in a report to the EPA in April of 2004, suggest that this phenomenon has the potential to occur approximately every 10 years and may impact sediments in certain portions of the river under all remedial scenarios. The EPA informed Alcoa that a final remedial decision for the river could not be made without substantially more information, including river pilot studies on the effects of ice formation and breakup on each of the remedial techniques. Alcoa submitted to the EPA and the EPA approved a Remedial Options Pilot Study (ROPS) to gather this information. The scope of this study includes sediment removal and capping, the installation of an ice control structure, and significant monitoring.

In May of 2004, Alcoa agreed to perform the study at an estimated cost of $35. Most of the construction work was completed in 2005 with monitoring proposed for 2006. The findings will be incorporated into a revised Analysis of Alternatives Report, which is expected to be submitted in 2007. This information will be used by the EPA to propose a remedy for the entire river.

Alcoa adjusted the reserves in the second quarter of 2004 to include the $35 for the ROPS. This is in addition to the $30 previously reserved. With the exception of the natural recovery remedy, none of the existing alternatives in the 2002 Analysis of Alternatives Report is more probable than the others and the results of the ROPS are necessary to revise the scope and estimated cost of many of the current alternatives.

The EPA’s ultimate selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA’s Record of Decision is issued, which is expected in 2007 or later.

Sherwin, TX. In connection with the sale of the Sherwin alumina refinery in Texas, which was required to be divested as part of the Reynolds merger in 2000, Alcoa has agreed to retain responsibility for the remediation of then existing environmental conditions, as well as a pro rata share of the final closure of the active waste disposal areas, which remain in use. Alcoa’s share of the closure costs is proportional to the total period of operation of the active waste disposal areas. Alcoa estimated its liability for the active disposal areas by making certain assumptions about the period of operation, the amount of material placed in the area prior to closure, and the appropriate technology, engineering, and regulatory status applicable to final closure. The most probable cost for remediation has been reserved. It is reasonably possible that an additional liability, not expected to exceed $75, may be incurred if actual experience varies from the original assumptions used.

East St. Louis, IL. In response to questions regarding environmental conditions at the former East St. Louis, IL operations, Alcoa entered into an administrative order with the EPA in December 2002 to perform a remedial investigation and feasibility study of an area used for the disposal of bauxite residue from historic alumina refining operations. A draft feasibility study was submitted to the EPA in April 2005. The feasibility study includes remedial alternatives that range from no further action at $0 to significant grading, stabilization, and water management of the bauxite residue disposal areas at $75. Because the selection of the $0 alternative was considered remote, Alcoa increased the environmental reserve for this location by $15 in the second quarter of 2005, representing the low end of the range of possible alternatives which meets the remedy selection criteria, as no alternative could be identified as more probable than the others. The EPA has not completed a final review of the feasibility study and the EPA’s selection of a remedy could result in additional liability. Alcoa may be required to record a subsequent reserve adjustment at the time the EPA’s Record of Decision is issued.

Based on the foregoing, it is possible that Alcoa's results of operations, in a particular period, could be materially affected by matters relating to these sites. However, based on facts currently available, management believes that adequate reserves have been provided and that the disposition of these matters will not have a materially adverse effect on the financial position or liquidity of the company.

Alcoa's remediation reserve balance was $353 and $390 at June 30, 2006 and December 31, 2005 (of which $51 and $40 was classified as a current liability), respectively, and reflects the most probable

costs to remediate identified environmental conditions for which costs can be reasonably estimated. In the first half of 2006, the remediation reserve was decreased by approximately $17 primarily due to an adjustment for the liabilities at Russian fabricating facilities acquired in January 2005. This adjustment was made after further investigations were completed whereby Alcoa was able to obtain additional information about the environmental condition and the associated liabilities with these facilities. This adjustment was recorded as an opening balance sheet adjustment and had no impact on net income. Payments related to remediation expenses were approximately $20 in the first half of 2006. These amounts include expenditures currently mandated, as well as those not required by any regulatory authority or third party.

Included in annual operating expenses are the recurring costs of managing hazardous substances and environmental programs. These costs are estimated to be about 2% of cost of goods sold.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

In addition to the risks inherent in its operations, Alcoa is exposed to financial, market, political and economic risks. The following discussion provides information regarding Alcoa's exposure to the risks of changing commodity prices, foreign exchange rates, and interest rates.

Alcoa's derivative activities are subject to the management, direction, and control of the Strategic Risk Management Committee (SRMC). The SRMC is composed of the chief executive officer, the chief financial officer, and other officers and employees that the chief executive officer selects. The SRMC reports to the Board of Directors on the scope of its activities.

The interest rate, foreign currency, aluminum and other commodity contracts are held for purposes other than trading. They are used primarily to mitigate uncertainty and volatility, and to cover underlying exposures. The company is not involved in energy-trading activities, weather derivatives, or other nonexchange commodity-trading activities.

Commodity Price Risks – Alcoa is a leading global producer of primary aluminum products and aluminum fabricated products. As a condition of sale, customers often require Alcoa to enter into long-term, fixed-price commitments. These commitments expose Alcoa to the risk of higher aluminum prices between the time the order is committed and the time that the order is shipped. Alcoa also sells aluminum products to third parties at then-current market prices and is exposed to the risk of lower market prices at the time of shipment. Alcoa uses futures and option contracts, totaling approximately 720,000 mt at June 30, 2006, to reduce the aluminum price risk of these exposures. The effects of this hedging activity will be recognized in earnings over the designated hedge periods, generally within four years.

Alcoa has also entered into futures and option contracts, totaling approximately 331,000 metric tons at June 30, 2006, to hedge a portion of future production. The effect of this hedging activity will be recognized in earnings over the designated hedge periods in 2006 to 2010.

Alcoa has also entered into certain derivatives to minimize its price risk related to other customer sales and pricing arrangements. Alcoa has not qualified these contracts for hedge accounting treatment, and therefore, the fair value gains and losses on these contracts are recorded in earnings. These contracts totaled 128,000 mt at June 30, 2006. In addition, Alcoa has entered into power supply and other contracts that contain pricing provisions related to the LME aluminum price. The LME-linked pricing features are considered embedded derivatives. A majority of these embedded derivatives have been designated as hedges of future sales of aluminum. Gains and losses on the remainder of these embedded derivatives are recognized in earnings.

The net mark-to-market pre-tax earnings impact from aluminum derivative and hedging activities was a gain of approximately $3 in the 2006 second quarter and a loss of $15 in the six-month period. The loss in the six-month period was principally due to an embedded LME derivative in a power contract.

Alcoa purchases natural gas, fuel oil, and electricity to meet its production requirements and believes it is highly likely that such purchases will continue in the future. These purchases expose the company to the risk of higher prices. To hedge a portion of these risks, Alcoa uses futures and forward contracts. The effects of this hedging activity will be recognized in earnings over the designated hedge periods, generally within five years.

Financial Risk

Interest rates – Alcoa uses interest rate swaps to help maintain a strategic balance between fixed- and floating-rate debt and to manage overall financing costs. For a portion of its fixed-rate debt, the company has entered into pay floating, receive fixed interest rate swaps to effectively change the fixed interest rates to floating interest rates.

Currencies – Alcoa is subject to exposure from fluctuations in foreign currency exchange rates. Foreign currency exchange contracts may be used from time to time to hedge the variability in cash flows from the forecasted payment or receipt of currencies other than the functional currency. These contracts cover periods consistent with known or expected exposures, generally not exceeding three years.

Fair values – The following table shows the fair values of outstanding derivatives contracts at June 30, 2006.

	Fair value gain/(loss)
Aluminum	$ (330)
Interest rates	(190)
Other commodities	(16)
Currencies	96

Aluminum consists primarily of losses on embedded derivatives in power contracts in Iceland and Brazil and our share of losses on hedge contracts of Norwegian smelters that are accounted for under the equity method.

Material Limitations - The disclosures with respect to commodity prices, interest rates, and foreign exchange risk do not take into account the underlying commitments or anticipated transactions. If the underlying items were included in the analysis, the gains or losses on the futures contracts may be offset. Actual results will be determined by a number of factors that are not under Alcoa's control and could vary significantly from those factors disclosed.

Alcoa is exposed to credit loss in the event of nonperformance by counterparties on the above instruments, as well as credit or performance risk with respect to its hedged customers' commitments. Although nonperformance is possible, Alcoa does not anticipate nonperformance by any of these parties. Futures contracts are with creditworthy counterparties and are further supported by cash, treasury bills, or irrevocable letters of credit issued by carefully chosen banks. In addition, various master netting arrangements are in place with each counterparty to facilitate settlement of gains and losses on these contracts.

Item 4. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures

Alcoa's Chief Executive Officer and Chief Financial Officer have evaluated the company's disclosure controls and procedures as of the end of the period covered by this report, and they have concluded that these controls and procedures are effective.

(b) Changes in Internal Control Over Financial Reporting

There have been no changes in Alcoa's internal control over financial reporting during the six-month period ended June 30, 2006, that have materially affected, or are reasonably likely to materially affect, the registrant's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

As previously reported, in May through October 2002, eleven lawsuits were filed against Reynolds Metals Company (Reynolds) and Alcoa in the District Court of Wharton County, Texas and one in the United States District Court, Southern District of Texas, Victoria Division. The lawsuits sought to recover damages relating to the presence of trichloroethylene in the groundwater near a former Reynolds extrusion facility in El Campo, Texas. Four of the cases were later dismissed and the remaining cases were consolidated into a single case in the District Court of Wharton County, Texas. Bon L Campo Limited Partnership and its parent, Tredegar Corporation, operators of the plant from 1997-2000, have also been listed among the defendants in some of the lawsuits. The only significant personal injury claim was settled in 2003. Alcoa, on behalf of itself, Reynolds, a Reynolds subsidiary, Bon L Campo LP, and Tredegar, has settled the claims of nearly all remaining plaintiffs, whose property is affected by the groundwater, including through the installation and operation of an extension of the City of El Campo water system using funds provided by Alcoa. Summary judgment was granted against the plaintiffs who did not own property affected by the groundwater. One group of these plaintiffs has filed an appeal of that summary judgment in No. 13-06-00240-CV in the 13th District Court of Appeals at Corpus Christi, Texas. Reynolds sued its predecessor in interest, Whitaker Corporation, seeking contribution toward the environmental cleanup of the facility. In March 2006 Alcoa and Whitaker reached a settlement whereby Whitaker will pay Alcoa a share of previous cleanup expenditures in installments to be completed by August 2006. Whitaker has also agreed to assume responsibility for the cleanup project under oversight by the State of Texas and Alcoa has agreed to reimburse to Whitaker a share of the future cleanup costs.

As previously reported, in 2002, Alcoa discovered that a former Reynolds distribution business sold approximately 750,000 pounds of aluminum plate made by unrelated companies for use in the Northwest maritime industry that is not suitable for that use. Reynolds notified the U.S. Coast Guard of the issue and worked cooperatively with it to identify and notify customers of the defective metal. An inspection process was employed to evaluate the identified metal and permit remedial efforts and settlements with affected boat builders and owners. All of the lawsuits previously filed by ship owners or operators have been resolved. As of the fourth quarter of 2005, all boats for which potential claims were anticipated have been identified and resolutions have been agreed to. During 2004, Alcoa reached resolution of a coverage suit with one of its carriers and used a portion of the proceeds to establish a reserve to cover the expected remaining claims. The suit filed against the manufacturers and sellers of the material was tried before a Washington State federal jury in May 2006 resulting in a judgment in favor of Alcoa totaling $75.7 million, including the prejudgment interest awarded by the court following the jury's verdict. In July 2006, prior to the expiration of the period for appeal of the judgment the parties agreed to a settlement of the matter and dismissal of any further court proceedings. Alcoa and its insurers continue to discuss the proper allocation of the settlement funds. No gain has been recorded in the financial statements due to the uncertainty associated with the final settlement.

On April 5, 2006, Alcoa was notified by the Court of Venice (Tribunal di Venezia) that Alcoa Trasformazioni S.r.l., Fusina site (Venice), was sued by the Italian Minister of Environment and Minister of Public Works for an alleged liability for environmental damages. The plaintiffs asserted that Alcoa, as present owner of the site contaminated by previous activities, had the duty to act promptly to prevent the site from contaminating the Venice Lagoon and its surrounding natural resources. Alcoa Trasformazioni denies responsibility for the pre-existing condition and for failing to eliminate or circumscribe the pollution which was already the object of initiatives by the public authorities and a clear duty of the previous owner and plant seller. Alcoa has sued Alumix and Efim (the sellers of the Fusina site) before the Court of Rome for indemnification against any liability related to the pollution of former Alumix sites, purchased by Alcoa in 1996. Plaintiffs seek compensation for damages to the environment plus costs of installing a physical barrier along the plant's border with the Lagoon.

On June 26, 2006, Alcoa Aluminio S.A. (Alcoa Aluminio) received a Notice of Violation and Fine from Brazil's Federal Revenue Department seeking payment of an isolated fine for alleged non-anticipation of payment of annual Corporate Income (CI) and Social Contribution Taxes (SCT), calculated under the presumed monthly taxable income mechanism. The claim is based on Alcoa Aluminio's not qualifying for the alternative method of anticipation of payment of CI and SCT used by the company, consisting of calculating such anticipations based on the actual taxable income mechanism, in accordance with applicable legislation. The claim seeks payment of Brazilian Real $669 million (equivalent to approximately US$304 million) and encompasses fiscal years from 2000 to 2005. Alcoa Aluminio believes that the claim is without merit and will present its defenses at all appropriate levels—administrative or judicial - of the Brazilian legal system.

The U.S. Environmental Protection Agency, the U.S. Department of Justice (DOJ), three citizens groups and Alcoa entered into a consent decree in 2003 in order to settle alleged violations of the Clean Air Act at Alcoa's Rockdale, Texas power plant. The consent decree was executed by Alcoa on March 27, 2003 and lodged with the U.S. District Court for the Western District of Texas on April 19, 2003. The court ordered entry of the consent decree on July 28, 2003. On July 18, 2006, pursuant to the terms of the consent decree, DOJ submitted a demand for stipulated penalties for alleged violations of opacity and sulphur dioxide limits at the power plant. The total demand for stipulated penalties is $9.2 million. Alcoa will contest the demand through the dispute resolution provisions of the consent decree.

On July 20, 2006, the European Commission (EC) announced that it has opened an investigation to establish whether an extension of the regulated preferential electricity tariff granted by Italy to some energy intensive industries complies with EC Treaty state aid rules. The new Italian power tariff modifies the preferential tariff that was in force until December 31, 2005 and extends it through 2010. Alcoa has been operating in Italy for more than 10 years under a power supply structure approved by the EU Commission in 1996. That measure, like the new one, was based on Italian state legislation that provides a competitive power supply to the primary aluminum industry and is not considered state aid by the Italian Government. The Commission’s announcement states that it has doubts about the measure’s compatibility with EU legislation and concerns about distortion of competition in the European market of primary aluminum, where energy is an important part of the production costs. The opening of an in-depth investigation gives interested parties the opportunity to comment on the proposed measures. It does not prejudge the outcome of the procedure. It is Alcoa’s understanding that the Italian Government’s continuation of the electricity tariff was done in conformity with all applicable laws and regulations. Alcoa believes that the total potential impact from a loss of the tariff would be approximately pre-tax $17 million per month in higher power costs at its Italian smelters.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

(c) Issuer Purchases of Equity Securities:

Period	Total Number of Shares Purchased (a)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Repurchase Plans or Programs (b)	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs (b)
January 1 - January 31, 2006	48,982	$30.24	—	26,200,282
February 1 - February 28, 2006	1,479,800	$30.03	1,479,800	24,720,482
March 1 - March 31, 2006	528,412	$29.90	520,200	24,200,282
Total for quarter ended March 31, 2006	2,057,194	$30.00	2,000,000	24,200,282
April 1 – April 30, 2006	2,066,050	$33.92	2,000,000	22,200,282
May 1 – May 31, 2006	2,636,111	$31.54	2,600,000	19,600,282
June 1 – June 30, 2006	—	—	—	19,600,282
Total for quarter ended June 30, 2006	4,702,161	$32.59	4,600,000	19,600,282

(a) This column includes (i) purchases under Alcoa's publicly announced share repurchase program described in (b) below and (ii) the deemed surrender to the company by plan participants of shares of common stock to satisfy the exercise price related to the exercise of employee stock options, in each case to the extent applicable during the period indicated. The shares used to satisfy the exercise price related to stock options are not considered part of the publicly announced share repurchase program approved by Alcoa's Board of Directors as described in (b) below.

(b) Alcoa's share repurchase program was approved by Alcoa's Board of Directors and publicly announced on July 13, 2001. The program authorizes the repurchase of up to 50 million shares of Alcoa common stock from time to time, directly or through brokers or agents, and has no expiration date.

Item 4. Submission of Matters to a Vote of Security Holders.

Information called for by this item with respect to the annual meeting of Alcoa shareholders held on April 21, 2006, is contained in Part II – Item 4 of Alcoa's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.

Item 6. Exhibits.

12. Computation of Ratio of Earnings to Fixed Charges

31. Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32. Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

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

Alcoa Inc.

July 26, 2006	By /s/ JOSEPH C. MUSCARI
Date	Joseph C. Muscari Executive Vice President and Chief Financial Officer (Principal Financial Officer)
July 26, 2006	By /s/ CHARLES D. MCLANE, JR.
Date	Charles D. McLane, Jr. Vice President - Corporate Controller (Principal Accounting Officer)

EXHIBITS

12. Computation of Ratio of Earnings to Fixed Charges
31. Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32. Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

EXHIBIT 12

Alcoa and subsidiaries

Computation of Ratio of Earnings to Fixed Charges
For the six months ended June 30, 2006
(in millions, except ratio)

Six months ended June 30	2006
Earnings:	
Income from continuing operations before taxes on income	$2,215
Minority interests' share of earnings of majority-owned subsidiaries without fixed charges	—
Equity income	(46)
Fixed charges	217
Distributed income of less than 50%-owned persons	13
Amortization of capitalized interest	11
Total earnings	$2,410
Fixed Charges:	
Interest expense:	
Consolidated	$ 190
Proportionate share of 50%-owned persons	3
	$ 193
Amount representative of the interest factor in rents:	
Consolidated	$ 23
Proportionate share of 50%-owned persons	1
	$ 24
Fixed charges added to earnings	$ 217
Interest capitalized:	
Consolidated	$ 54
Proportionate share of 50%-owned persons	—
	$ 54
Preferred stock dividend requirements of majority-owned subsidiaries	—
Total fixed charges	$ 271
Ratio of earnings to fixed charges	8.9

EXHIBIT 31

Certifications

I, Alain J. P. Belda, Chairman of the Board and Chief Executive Officer of Alcoa Inc., certify that:

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

Date: July 26, 2006

/s/ ALAIN J. P. BELDA

Title: Chairman of the Board and
Chief Executive Officer

I, Joseph C. Muscari, Executive Vice President and Chief Financial Officer of Alcoa Inc., certify that:

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

Date: July 26, 2006

/s/ JOSEPH C. MUSCARI

Title: Executive Vice President and
Chief Financial Officer

EXHIBIT 32

Certification
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), each of the undersigned officers of Alcoa Inc., a Pennsylvania corporation (the "Company"), does hereby certify that:

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

Dated: July 26, 2006

/s/ ALAIN J. P. BELDA
Name: Alain J. P. Belda
Title: Chairman of the Board and Chief Executive Officer

Dated: July 26, 2006

/s/ JOSEPH C. MUSCARI
Name: Joseph C. Muscari
Title: Executive Vice President and Chief Financial Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished to the Securities and Exchange Commission as an exhibit to the Form 10-Q and shall not be considered filed as part of the Form 10-Q.

EXHIBIT 99.6

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON FINANCIAL STATEMENT SCHEDULE

To the Board of Directors
of Alcoa Inc.:

Our audits of the consolidated financial statements, of management's assessment of the effectiveness of internal control over financial reporting and of the effectiveness of internal control over financial reporting referred to in our report dated February 17, 2006, except with respect to our opinion on the consolidated financial statements insofar as it relates to the effects of the discontinued operations discussed in Note B, as to which the date is January 15, 2007, appearing in the 2005 Annual Report to Shareholders of Alcoa Inc. and its subsidiaries (which report, consolidated financial statements and assessment are incorporated by reference in this Annual Report on Form 10-K) also included an audit of the financial statement schedule included in this Current Report on Form 8-K. In our opinion, this financial statement schedule presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

/s/ PricewaterhouseCoopers LLP

Pittsburgh, Pennsylvania
February 17, 2006, except with respect to the effects of the discontinued operations discussed in Note B to the consolidated financial statements, as to which the date is January 15, 2007