

KEYCORP /NEW/  
Form 10-Q  
May 05, 2016  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington D.C. 20549**

**Form 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the Quarterly Period Ended March 31, 2016**  
**Commission File Number 001-11302**

**Exact name of registrant as specified in its charter:**

**Ohio**

**34-6542451**

<b>State or other jurisdiction of incorporation or organization</b>	<b>I.R.S. Employer Identification Number:</b>
<b>127 Public Square, Cleveland, Ohio</b>	<b>44114-1306</b>
<b>Address of principal executive offices:</b>	<b>Zip Code:</b>
<b>(216) 689-3000</b>	

**Registrant's telephone number, including area code:**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

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

Common Shares with a par value of \$1 each	842,372,999 Shares
<b>Title of class</b>	<b>Outstanding at May 2, 2016</b>

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Throughout the Notes to Consolidated Financial Statements (Unaudited) and Management's Discussion & Analysis of Financial Condition & Results of Operations, we use certain acronyms and abbreviations as defined in Note 1 ( **Basis of Presentation and Accounting Policies** ) that begins on page 10.

**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****Consolidated Balance Sheets**

<i>in millions, except per share data</i>	<b>March 31, 2016 (Unaudited)</b>	<b>December 31, 2015</b>	<b>March 31, 2015 (Unaudited)</b>
<b>ASSETS</b>			
Cash and due from banks	\$ 474	\$ 607	\$ 506
Short-term investments	5,436	2,707	3,378
Trading account assets	765	788	789
Securities available for sale	14,304	14,218	13,120
Held-to-maturity securities (fair value: \$5,031, \$4,848, and \$5,003)	5,003	4,897	5,005
Other investments	643	655	730
Loans, net of unearned income of \$623, \$646, and \$665	60,438	59,876	57,953
Less: Allowance for loan and lease losses	826	796	794
Net loans	59,612	59,080	57,159
Loans held for sale	684	639	1,649
Premises and equipment	750	779	806
Operating lease assets	362	340	306
Goodwill	1,060	1,060	1,057
Other intangible assets	57	65	92
Corporate-owned life insurance	3,557	3,541	3,488
Derivative assets	1,065	619	731
Accrued income and other assets	2,849	3,292	3,142
Discontinued assets (including \$3, \$4, and \$187 million of portfolio loans at fair value, see Note 11)	1,781	1,846	2,246
Total assets	\$ 98,402	\$ 95,133	\$ 94,204
<b>LIABILITIES</b>			
Deposits in domestic offices:			
NOW and money market deposit accounts	\$ 38,946	\$ 37,089	\$ 35,623
Savings deposits	2,385	2,341	2,413
Certificates of deposit (\$100,000 or more)	3,095	2,392	1,982
Other time deposits	3,259	3,127	3,182
Total interest-bearing deposits	47,685	44,949	43,200
Noninterest-bearing deposits	25,697	26,097	27,948
Deposits in foreign office interest-bearing			474
Total deposits	73,382	71,046	71,622

Federal funds purchased and securities sold under repurchase agreements	374	372	517
Bank notes and other short-term borrowings	615	533	608
Derivative liabilities	790	632	825
Accrued expense and other liabilities	1,410	1,605	1,308
Long-term debt	10,760	10,186	8,711
<b>Total liabilities</b>	<b>87,331</b>	<b>84,374</b>	<b>83,591</b>
<b>EQUITY</b>			
Preferred stock, \$1 par value, authorized 25,000,000 shares:			
7.75% Noncumulative Perpetual Convertible Preferred Stock, Series A, \$100 liquidation preference; authorized 7,475,000 shares; issued 2,900,234, 2,900,234, and 2,900,234 shares			
	290	290	290
Common shares, \$1 par value; authorized 1,400,000,000 shares; issued 1,016,969,905, 1,016,969,905, and 1,016,969,905 shares			
	1,017	1,017	1,017
Capital surplus	3,818	3,922	3,910
Retained earnings	9,042	8,922	8,445
Treasury stock, at cost (174,680,274, 181,218,648, and 166,049,974 shares)			
	(2,888)	(3,000)	(2,780)
Accumulated other comprehensive income (loss)			
	(213)	(405)	(279)
Key shareholders equity	11,066	10,746	10,603
Noncontrolling interests	5	13	10
<b>Total equity</b>	<b>11,071</b>	<b>10,759</b>	<b>10,613</b>
<b>Total liabilities and equity</b>	<b>\$ 98,402</b>	<b>\$ 95,133</b>	<b>\$ 94,204</b>

See Notes to Consolidated Financial Statements (Unaudited).

**Table of Contents****Consolidated Statements of Income (Unaudited)**

<i>dollars in millions, except per share amounts</i>	<b>Three months ended March 31,</b>	
	<b>2016</b>	<b>2015</b>
<b>INTEREST INCOME</b>		
Loans	\$ 562	\$ 523
Loans held for sale	8	7
Securities available for sale	75	70
Held-to-maturity securities	24	24
Trading account assets	7	5
Short-term investments	4	2
Other investments	3	5
<b>Total interest income</b>	<b>683</b>	<b>636</b>
<b>INTEREST EXPENSE</b>		
Deposits	31	26
Bank notes and other short-term borrowings	2	2
Long-term debt	46	37
<b>Total interest expense</b>	<b>79</b>	<b>65</b>
<b>NET INTEREST INCOME</b>		
Provision for credit losses	89	35
<b>Net interest income after provision for credit losses</b>	<b>515</b>	<b>536</b>
<b>NONINTEREST INCOME</b>		
Trust and investment services income	109	109
Investment banking and debt placement fees	71	68
Service charges on deposit accounts	65	61
Operating lease income and other leasing gains	17	19
Corporate services income	50	43
Cards and payments income	46	42
Corporate-owned life insurance income	28	31
Consumer mortgage income	2	3
Mortgage servicing fees	12	13
Net gains (losses) from principal investing		29
Other income <sup>(a)</sup>	31	19
<b>Total noninterest income</b>	<b>431</b>	<b>437</b>
<b>NONINTEREST EXPENSE</b>		
Personnel	404	389
Net occupancy	61	65
Computer processing	43	38
Business services and professional fees	41	33



Equipment	21	22
Operating lease expense	13	11
Marketing	12	8
FDIC assessment	9	8
Intangible asset amortization	8	9
OREO expense, net	1	2
Other expense	90	84
<b>Total noninterest expense</b>	<b>703</b>	<b>669</b>
<b>INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES</b>	<b>243</b>	<b>304</b>
Income taxes	56	74
<b>INCOME (LOSS) FROM CONTINUING OPERATIONS</b>	<b>187</b>	<b>230</b>
Income (loss) from discontinued operations, net of taxes of \$0 and \$3 (see Note 11)	1	5
<b>NET INCOME (LOSS)</b>	<b>188</b>	<b>235</b>
Less: Net income (loss) attributable to noncontrolling interests		2
<b>NET INCOME (LOSS) ATTRIBUTABLE TO KEY</b>	<b>\$ 188</b>	<b>\$ 233</b>
Income (loss) from continuing operations attributable to Key common shareholders	\$ 182	\$ 222
Net income (loss) attributable to Key common shareholders	183	227
Per common share:		
Income (loss) from continuing operations attributable to Key common shareholders	\$ .22	\$ .26
Income (loss) from discontinued operations, net of taxes		.01
Net income (loss) attributable to Key common shareholders <sup>(b)</sup>	.22	.27
Per common share assuming dilution:		
Income (loss) from continuing operations attributable to Key common shareholders	\$ .22	\$ .26
Income (loss) from discontinued operations, net of taxes		.01
Net income (loss) attributable to Key common shareholders <sup>(b)</sup>	.22	.26
Cash dividends declared per common share	\$ .075	\$ .065
Weighted-average common shares outstanding (000) <sup>(c)</sup>	827,381	848,580
Effect of convertible preferred stock		
Effect of common share options and other stock awards <sup>(c)</sup>	7,679	8,542
Weighted-average common shares and potential common shares outstanding (000) <sup>(c), (d)</sup>	835,060	857,122

- (a) For the three months ended March 31, 2016, and March 31, 2015, net securities gains (losses) totaled less than \$1 million. For the three months ended March 31, 2016, we did not have any impairment losses related to securities. For the three months ended March 31, 2015, impaired losses related to securities

totaled less than \$1 million.

- (b) EPS may not foot due to rounding.
- (c) For the three months ended March 31, 2016, weighted-average common shares outstanding, effect of common share options and other stock awards, and weighted-average common shares and potential common shares outstanding have been revised from our financial results reported on Form 8-K on April 21, 2016.
- (d) Assumes conversion of common share options and other stock awards and/or convertible preferred stock, as applicable.

See Notes to Consolidated Financial Statements (Unaudited).

**Table of Contents****Consolidated Statements of Comprehensive Income (Unaudited)**

<i>in millions</i>	<b>Three months ended March 31,</b>	
	<b>2016</b>	<b>2015</b>
Net income (loss)	\$ 188	\$ 235
Other comprehensive income (loss), net of tax:		
Net unrealized gains (losses) on securities available for sale, net of income taxes of \$76 and \$33	128	55
Net unrealized gains (losses) on derivative financial instruments, net of income taxes of \$34 and \$19	58	32
Foreign currency translation adjustments, net of income taxes of \$3 and (\$8)	5	(13)
Net pension and postretirement benefit costs, net of income taxes of \$4 and \$1	1	3
Total other comprehensive income (loss), net of tax	192	77
Comprehensive income (loss)	380	312
Less: Comprehensive income attributable to noncontrolling interests		2
Comprehensive income (loss) attributable to Key	\$ 380	\$ 310

See Notes to Consolidated Financial Statements (Unaudited).

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## Consolidated Statements of Changes in Equity (Unaudited)

	Key Shareholders Equity						Accumulated Other Comprehensive Income	Treasury Stock, at Cost	Noncontrolling Interests
	Preferred Shares Outstanding	Common Shares Outstanding	Preferred Stock	Common Shares	Capital Surplus	Retained Earnings			
<i>dollars in millions, except per share amounts</i>	(000)	(000)							
<b>BALANCE AT DECEMBER 31, 2014</b>	2,905	859,403	\$ 291	\$ 1,017	\$ 3,986	\$ 8,273	\$(2,681)	\$(356)	\$ 12
Net income (loss)						233			2
Other comprehensive income (loss):									
Net unrealized gains (losses) on securities available for sale, net of income taxes of \$33								55	
Net unrealized gains (losses) on derivative financial instruments, net of income taxes of \$19								32	
Foreign currency translation adjustments, net of income taxes of (\$8)								(13)	
Net pension and postretirement benefit costs, net of income taxes of \$1								3	
Deferred compensation					5				
Cash dividends declared on common shares (\$0.065 per share)							(55)		
Cash dividends declared on Noncumulative Series A Preferred Stock (\$1.9375 per share)							(6)		
Common shares repurchased		(14,087)					(197)		
Series A Preferred Stock exchanged for common shares	(5)	33	(1)				1		
Common shares reissued (returned) for stock options and other employee benefit plans		5,571				(81)	97		
Net contribution from (distribution to) noncontrolling interests									(4)
<b>BALANCE AT MARCH 31, 2015</b>	2,900	850,920	\$ 290	\$ 1,017	\$ 3,910	\$ 8,445	\$(2,780)	\$(279)	\$ 10
<b>BALANCE AT DECEMBER 31, 2015</b>	2,900	835,751	\$ 290	\$ 1,017	\$ 3,922	\$ 8,922	\$(3,000)	\$(405)	\$ 13
Net income (loss)						<b>188</b>			
Other comprehensive income (loss):									
Net unrealized gains (losses) on securities available for sale, net of income taxes of \$76								<b>128</b>	
Net unrealized gains (losses) on derivative financial instruments, net of income taxes of \$34								<b>58</b>	
Foreign currency translation adjustments, net of income taxes of \$3								<b>5</b>	
								<b>1</b>	

Net pension and postretirement benefit costs, net of income taxes of \$3										
Deferred compensation										(6)
Cash dividends declared on common shares (\$0.075 per share)										(63)
Cash dividends declared on Noncumulative Series A Preferred Stock (\$1.9375 per share)										(5)
Common shares reissued (returned) for stock options and other employee benefit plans	6,539								(98)	112
Net contribution from (distribution to) noncontrolling interests										(8)
<b>BALANCE AT MARCH 31, 2016</b>	<b>2,900</b>	<b>842,290</b>	<b>\$ 290</b>	<b>\$ 1,017</b>	<b>\$ 3,818</b>	<b>\$ 9,042</b>	<b>\$ (2,888)</b>	<b>\$ (213)</b>	<b>\$ 5</b>	

See Notes to Consolidated Financial Statements (Unaudited).

**Table of Contents****Consolidated Statements of Cash Flows (Unaudited)**

<i>in millions</i>	<b>Three months ended March 31,</b>	
	<b>2016</b>	<b>2015</b>
<b>OPERATING ACTIVITIES</b>		
Net income (loss)	\$ 188	\$ 235
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Provision for credit losses	89	35
Depreciation, amortization and accretion expense, net	62	50
Increase in cash surrender value of corporate-owned life insurance	(25)	(25)
Stock-based compensation expense	19	13
FDIC reimbursement (payments), net of FDIC expense	1	
Deferred income taxes (benefit)	50	50
Proceeds from sales of loans held for sale	1,110	1,225
Originations of loans held for sale, net of repayments	(1,153)	(2,109)
Net losses (gains) on sales of loans held for sale	(2)	(20)
Net losses (gains) from principal investing		(29)
Net losses (gains) and writedown on OREO	1	
Net losses (gains) on leased equipment		(3)
Net losses (gains) on sales of fixed assets	1	
Net decrease (increase) in trading account assets	23	(39)
Other operating activities, net	9	(485)
<b>NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES</b>	<b>373</b>	<b>(1,102)</b>
<b>INVESTING ACTIVITIES</b>		
Net decrease (increase) in short-term investments, excluding acquisitions	(2,729)	891
Purchases of securities available for sale	(610)	(403)
Proceeds from prepayments and maturities of securities available for sale	722	724
Proceeds from prepayments and maturities of held-to-maturity securities	251	266
Purchases of held-to-maturity securities	(358)	(257)
Purchases of other investments	(18)	(13)
Proceeds from sales of other investments	24	32
Proceeds from prepayments and maturities of other investments		4
Net decrease (increase) in loans, excluding acquisitions, sales and transfers	(663)	(727)
Proceeds from sales of portfolio loans	40	47
Proceeds from corporate-owned life insurance	9	15
Purchases of premises, equipment, and software	(8)	(3)
Proceeds from sales of OREO	3	6
<b>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</b>	<b>(3,337)</b>	<b>582</b>
<b>FINANCING ACTIVITIES</b>		
Net increase (decrease) in deposits, excluding acquisitions	2,336	(376)
Net increase (decrease) in short-term borrowings	84	127
Net proceeds from issuance of long-term debt	976	1,000
Payments on long-term debt	(498)	(129)

Repurchase of common shares			(197)
Net proceeds from reissuance of common shares	<b>1</b>		9
Cash dividends paid	<b>(68)</b>		(61)
<b>NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES</b>	<b>2,831</b>		373
<b>NET INCREASE (DECREASE) IN CASH AND DUE FROM BANKS</b>	<b>(133)</b>		(147)
<b>CASH AND DUE FROM BANKS AT BEGINNING OF PERIOD</b>	<b>607</b>		653
<b>CASH AND DUE FROM BANKS AT END OF PERIOD</b>	<b>\$ 474</b>	<b>\$</b>	506
Additional disclosures relative to cash flows:			
Interest paid	<b>\$ 108</b>	<b>\$</b>	98
Income taxes paid (refunded)	<b>13</b>		19
Noncash items:			
Reduction of secured borrowing and related collateral	<b>\$ 21</b>	<b>\$</b>	72
Loans transferred to held for sale from portfolio			10
Loans transferred to OREO	<b>4</b>		7
See Notes to Consolidated Financial Statements (Unaudited).			

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

**1. Basis of Presentation and Accounting Policies**

As used in these Notes, references to Key, we, our, us, and similar terms refer to the consolidated entity consisting of KeyCorp and its subsidiaries. KeyCorp refers solely to the parent holding company, and KeyBank refers to KeyCorp's subsidiary, KeyBank National Association.

The acronyms and abbreviations identified below are used in the Notes to Consolidated Financial Statements (Unaudited) as well as in the Management's Discussion & Analysis of Financial Condition & Results of Operations. You may find it helpful to refer back to this page as you read this report.

References to our 2015 Form 10-K refer to our Form 10-K for the year ended December 31, 2015, which was filed with the U.S. Securities and Exchange Commission and is available on its website ([www.sec.gov](http://www.sec.gov)) and on our website ([www.key.com/ir](http://www.key.com/ir)).

AICPA: American Institute of Certified Public Accountants.

ALCO: Asset/Liability Management Committee.

ALLL: Allowance for loan and lease losses.

A/LM: Asset/liability management.

AOCI: Accumulated other comprehensive income (loss).

APBO: Accumulated postretirement benefit obligation.

Austin: Austin Capital Management, Ltd.

BHCs: Bank holding companies.

Board: KeyCorp Board of Directors.

CCAR: Comprehensive Capital Analysis and Review.

CMBS: Commercial mortgage-backed securities.

CMO: Collateralized mortgage obligation.

Common shares: KeyCorp common shares, \$1 par value.

DIF: Deposit Insurance Fund of the FDIC.

Dodd-Frank Act: Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

EBITDA: Earnings before interest, taxes, depreciation, and amortization.

EPS: Earnings per share.

ERM: Enterprise risk management.

EVE: Economic value of equity.

FASB: Financial Accounting Standards Board.

FDIC: Federal Deposit Insurance Corporation.

Federal Reserve: Board of Governors of the Federal Reserve System.

FHLB: Federal Home Loan Bank of Cincinnati.

KCDC: Key Community Development Corporation.

KEF: Key Equipment Finance.

KPP: Key Principal Partners

KREEC: Key Real Estate Equity Capital, Inc.

LCR: Liquidity coverage ratio.

LIBOR: London Interbank Offered Rate.

LIHTC: Low-income housing tax credit.

Moody's: Moody's Investor Services, Inc.

MRM: Market Risk Management group.

N/A: Not applicable.

NASDAQ: The NASDAQ Stock Market LLC.

NAV: Net asset value.

N/M: Not meaningful.

NOW: Negotiable Order of Withdrawal.

NPR: Notice of proposed rulemaking.

NYSE: New York Stock Exchange.

OCC: Office of the Comptroller of the Currency.

OCI: Other comprehensive income (loss).

OREO: Other real estate owned.

OTTI: Other-than-temporary impairment.

PBO: Projected benefit obligation.

PCI: Purchased credit impaired.

S&P: Standard and Poor's Ratings Services, a Division of The

McGraw-Hill Companies, Inc.

SEC: U.S. Securities and Exchange Commission.

Series A Preferred Stock: KeyCorp's 7.75% Noncumulative



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FHLMC: Federal Home Loan Mortgage Corporation.  
First Niagara: First Niagara Financial Group, Inc.

(NASDAQ: FNFG).

FNMA: Federal National Mortgage Association, or Fannie Mae.

FSOC: Financial Stability Oversight Council.

GAAP: U.S. generally accepted accounting principles.

GNMA: Government National Mortgage Association.

ISDA: International Swaps and Derivatives Association.

KAHC: Key Affordable Housing Corporation.

KBCM: KeyBanc Capital Markets, Inc.

KCC: Key Capital Corporation.

Perpetual Convertible Preferred Stock, Series A.

SIFIs: Systemically important financial institutions, including

BHCs with total consolidated assets of at least \$50 billion

and nonbank financial companies designated by FSOC for

supervision by the Federal Reserve.

TDR: Troubled debt restructuring.

TE: Taxable-equivalent.

U.S. Treasury: United States Department of the Treasury.

VaR: Value at risk.

VEBA: Voluntary Employee Beneficiary Association.

VIE: Variable interest entity.

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The consolidated financial statements include the accounts of KeyCorp and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. Some previously reported amounts have been reclassified to conform to current reporting practices.

The consolidated financial statements include any voting rights entities in which we have a controlling financial interest. In accordance with the applicable accounting guidance for consolidations, we consolidate a VIE if we have: (i) a variable interest in the entity; (ii) the power to direct activities of the VIE that most significantly impact the entity's economic performance; and (iii) the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the VIE (i.e., we are considered to be the primary beneficiary). Variable interests can include equity interests, subordinated debt, derivative contracts, leases, service agreements, guarantees, standby letters of credit, loan commitments, and other contracts, agreements, and financial instruments. See Note 9 ( Variable Interest Entities ) for information on our involvement with VIEs.

We use the equity method to account for unconsolidated investments in voting rights entities or VIEs if we have significant influence over the entity's operating and financing decisions (usually defined as a voting or economic interest of 20% to 50%, but not controlling). Unconsolidated investments in voting rights entities or VIEs in which we have a voting or economic interest of less than 20% generally are carried at cost. Investments held by our registered broker-dealer and investment company subsidiaries (principal investing entities and Real Estate Capital line of business) are carried at fair value.

We believe that the unaudited consolidated interim financial statements reflect all adjustments of a normal recurring nature and disclosures that are necessary for a fair presentation of the results for the interim periods presented. The results of operations for the interim period are not necessarily indicative of the results of operations to be expected for the full year. The interim financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in our 2015 Form 10-K.

In preparing these financial statements, subsequent events were evaluated through the time the financial statements were issued. Financial statements are considered issued when they are widely distributed to all shareholders and other financial statement users, or filed with the SEC.

## **Offsetting Derivative Positions**

In accordance with the applicable accounting guidance, we take into account the impact of bilateral collateral and master netting agreements that allow us to settle all derivative contracts held with a single counterparty on a net basis, and to offset the net derivative position with the related cash collateral when recognizing derivative assets and liabilities. Additional information regarding derivative offsetting is provided in Note 7 ( Derivatives and Hedging Activities ).

## **Accounting Guidance Adopted in 2016**

**Business combinations.** In September 2015, the FASB issued new accounting guidance that obligates an acquirer in a business combination to recognize adjustments to provisional amounts in the reporting period that the amounts were determined, eliminating the requirement for retrospective adjustments. The acquirer should record in the current period any income effects that resulted from the change in provisional amounts, calculated as if the accounting were completed at the acquisition date. This accounting guidance was effective prospectively for interim and annual reporting periods beginning after December 15, 2015 (effective January 1, 2016, for us). Early adoption was permitted. The adoption of this accounting guidance did not affect our financial condition or results of operations.

***Fair value measurement.*** In May 2015, the FASB issued new disclosure guidance that eliminates the requirement to categorize investments measured using the net asset value practical expedient in the fair value hierarchy table. Entities are required to disclose the fair value of investments measured using the net asset value practical expedient so that financial statement users can reconcile amounts reported in the fair value hierarchy table to amounts reported on the balance sheet. This disclosure guidance was effective for interim and annual reporting periods beginning after December 15, 2015 (March 31, 2016, for us) on a retrospective basis. Early adoption was permitted. The adoption of this disclosure guidance did not affect our financial condition or results of operations. We provide the disclosure related to this new guidance in Note 5 ( Fair Value Measurements ).

***Cloud computing fees.*** In April 2015, the FASB issued new accounting guidance that clarifies a customer's accounting for fees paid in a cloud computing arrangement. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a

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service contract. This accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2015 (effective January 1, 2016, for us) and could be implemented using either a prospective method or a retrospective method. Early adoption was permitted. We elected to implement this new accounting guidance using a prospective approach. The adoption of this accounting guidance did not affect our financial condition or results of operations.

***Imputation of interest.*** In April 2015, the FASB issued new accounting guidance that requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This accounting guidance was effective retrospectively for interim and annual reporting periods beginning after December 15, 2015 (effective January 1, 2016, for us). Early adoption was permitted. The adoption of this accounting guidance did not have a material effect on our financial condition or results of operations.

***Consolidation.*** In February 2015, the FASB issued new accounting guidance that changes the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. The new guidance amends the current accounting guidance to address limited partnerships and similar legal entities, certain investment funds, fees paid to a decision maker or service provider, and the impact of fee arrangements and related parties on the primary beneficiary determination. This accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2015 (effective January 1, 2016, for us) and was implemented using a modified retrospective basis. Retrospective application to all relevant prior periods and early adoption was permitted. The adoption of this accounting guidance did not affect our financial condition or results of operations. Our Principal Investing unit and the Real Estate Capital line of business have equity and mezzanine investments, which were subjected to the new guidance. We determined these investments are VIEs. We provide disclosures related to our variable interest entities as required by the new guidance in Note 9 ( Variable Interest Entities ).

***Derivatives and hedging.*** In November 2014, the FASB issued new accounting guidance that clarifies how current guidance should be interpreted when evaluating the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. An entity should consider all relevant terms and features, including the embedded derivative feature being evaluated for bifurcation, when evaluating the nature of a host contract. This accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2015 (effective January 1, 2016, for us) and could be implemented using a modified retrospective basis. Retrospective application to all relevant prior periods and early adoption was permitted. The adoption of this accounting guidance did not affect our financial condition or results of operations.

***Consolidation.*** In August 2014, the FASB issued new accounting guidance that clarifies how to measure the financial assets and the financial liabilities of a consolidated collateralized financing entity. This accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2015 (effective January 1, 2016, for us) and could be implemented using either a retrospective method or a cumulative-effect approach. Early adoption was permitted. The adoption of this accounting guidance did not affect our financial condition or results of operations.

***Stock-based compensation.*** In June 2014, the FASB issued new accounting guidance that clarifies how to account for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period. This accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2015 (effective January 1, 2016, for us) and could be implemented using either a retrospective method or a prospective method. Early adoption was permitted. We elected to implement this new accounting guidance using a prospective approach. The adoption of this accounting guidance did not affect our financial condition or results of operations.

**Accounting Guidance Pending Adoption at March 31, 2016**

***Stock-based compensation.*** In March 2016, the FASB issued new accounting guidance that simplifies accounting for several aspects of share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and presentation on the statement of cash flows. This accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us). The method of transition is dependent on the particular amendment within the new guidance. Early adoption is permitted. We are currently evaluating the impact that this accounting guidance may have on our financial condition or results of operations.

***Equity method investments.*** In March 2016, the FASB issued new accounting guidance that simplifies the transition to equity method accounting by eliminating the requirement for an investor to make retroactive adjustments to the investment, results of operations, and retained earnings on a step-by-step basis when an investment becomes qualified for equity method accounting. Instead, when an investment qualifies for the equity method due to an increase in ownership or degree of

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influence, an equity method investor is required to add the cost of acquiring the additional interest to the current basis of the previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for the equity method. This accounting guidance will be effective prospectively for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us). Early adoption is permitted. The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

***Derivatives and hedging.*** In March 2016, the FASB issued new accounting guidance that requires an entity to use a four-step decision model when assessing contingent call (put) options that can accelerate the payment of principal on debt instruments to determine whether they are clearly and closely related to their debt hosts. This accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us) and must be implemented using a modified retrospective basis. Early adoption is permitted. The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

***Derivatives and hedging.*** In March 2016, the FASB issued new accounting guidance that clarifies that a change in the counterparty to a derivative instrument that has been designated as a hedging instrument does not, by itself, require dedesignation, but all other hedge accounting criteria must be met. This accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us) and can be implemented using either a prospective method or a modified retrospective method. Early adoption is permitted. We have elected to implement this new accounting guidance using a prospective method. The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

***Extinguishment of liabilities.*** In March 2016, the FASB issued new accounting guidance that clarifies that liabilities related to the sale of prepaid stored-value products are financial liabilities, and breakage should be accounted for under the breakage guidance in the new revenue recognition accounting guidance. It also provides clarity on how prepaid product liabilities should be derecognized. This accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us) and can be implemented using either a modified retrospective approach or retrospective approach. We are currently determining a transition method and evaluating the impact that this accounting guidance may have on our financial condition or results of operations.

***Leases.*** In February 2016, the FASB issued new accounting guidance that requires a lessee to recognize a liability to make lease payments and a right of use asset representing its right to use an underlying asset during the lease term for both finance and operating leases. The definition of a lease was modified to exemplify the concept of control over an asset identified in the lease. Lease classification criteria remains substantially similar to criteria in current lease guidance. The guidance defines which payments can be used in determining lease classification. For short-term leases with a term of 12 months or less, lessees can make a policy election not to recognize lease assets and lease liabilities. Lessor accounting is largely unchanged. Leveraged leases that commenced before the effective date of the new guidance are grandfathered. New disclosures are required, and certain practical expedients are allowed upon adoption. This accounting and disclosure guidance will be effective for interim and annual reporting periods beginning after December 15, 2018 (effective January 1, 2019, for us) and should be implemented using the modified retrospective approach. Early adoption is permitted. We are currently evaluating the impact that this accounting guidance may have on our financial condition or results of operations.

***Financial instruments.*** In January 2016, the FASB issued new accounting guidance that requires equity investments, except those accounted for under the equity method of accounting or consolidated, to be measured at fair value with changes recognized in net income. If there is no readily determinable fair value, the guidance allows entities the ability to measure investments at cost less impairment, whereby impairment is based on a qualitative assessment. The

guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost and changes the presentation of financial assets and financial liabilities on the balance sheet or in the footnotes. If an entity has elected the fair value option to measure liabilities, the new accounting guidance requires the portion of the change in the fair value of a liability resulting from credit risk to be presented in OCI. We have not elected to measure any of our liabilities at fair value, and therefore, this aspect of the guidance is not applicable to us. This accounting and disclosure guidance will be effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us). For the guidance applicable to us, the accounting will be implemented on a prospective basis, whereby early adoption is not permitted. We are currently evaluating the impact that this accounting guidance may have on our financial condition or results of operations.

**Going concern.** In August 2014, the FASB issued new accounting guidance that requires management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date the financial statements are issued. Disclosure is required when conditions or events raise substantial doubt about an entity's ability to

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continue as a going concern. This accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us). Early adoption is permitted. The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

**Revenue recognition.** In May 2014, the FASB issued new accounting guidance that revises the criteria for determining when to recognize revenue from contracts with customers and expands disclosure requirements. This accounting guidance can be implemented using either a retrospective method or a cumulative-effect approach. In August 2015, the FASB issued an update that defers the effective date of the revenue recognition guidance by one year. This new guidance will be effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us). Early adoption is permitted but only for interim and annual reporting periods beginning after December 15, 2016. We have elected to implement this new accounting guidance using a cumulative-effect approach. Our preliminary analysis suggests that the adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations. There are many aspects of this new accounting guidance that are still being interpreted, and the FASB has recently issued updates to certain aspects of the guidance to address implementation issues. For example, the FASB issued accounting guidance in March 2016 to clarify principal versus agent considerations and additional guidance in April 2016 to clarify the identification of performance obligations and the licensing implementation guidance. The results of our materiality analysis may change based on the conclusions reached as to the application of the new guidance.



Table of Contents**2. Earnings Per Common Share**

Basic earnings per share is the amount of earnings (adjusted for dividends declared on our preferred stock) available to each common share outstanding during the reporting periods. Diluted earnings per share is the amount of earnings available to each common share outstanding during the reporting periods adjusted to include the effects of potentially dilutive common shares. Potentially dilutive common shares include incremental shares issued for the conversion of our convertible Series A Preferred Stock, stock options, and other stock-based awards. Potentially dilutive common shares are excluded from the computation of diluted earnings per share in the periods where the effect would be antidilutive. For diluted earnings per share, net income available to common shareholders can be affected by the conversion of our convertible Series A Preferred Stock. Where the effect of this conversion would be dilutive, net income available to common shareholders is adjusted by the amount of preferred dividends associated with our Series A Preferred Stock.

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

<i>dollars in millions, except per share amounts</i>	<b>Three months ended March 31,</b>	
	<b>2016</b>	<b>2015</b>
<b>EARNINGS</b>		
Income (loss) from continuing operations	\$ 187	\$ 230
Less: Net income (loss) attributable to noncontrolling interests		2
Income (loss) from continuing operations attributable to Key	187	228
Less: Dividends on Series A Preferred Stock	5	6
Income (loss) from continuing operations attributable to Key common shareholders	182	222
Income (loss) from discontinued operations, net of taxes (a)	1	5
Net income (loss) attributable to Key common shareholders	\$ 183	\$ 227
<b>WEIGHTED-AVERAGE COMMON SHARES</b>		
Weighted-average common shares outstanding (000) (b)	827,381	848,580
Effect of convertible preferred stock		
Effect of common share options and other stock awards (b)	7,679	8,542
Weighted-average common shares and potential common shares outstanding (000) (b), (c)	835,060	857,122
<b>EARNINGS PER COMMON SHARE</b>		
	\$ .22	\$ .26

Income (loss) from continuing operations attributable to Key common shareholders			
Income (loss) from discontinued operations, net of taxes (a)			.01
Net income (loss) attributable to Key common shareholders (d)	.22		.27
Income (loss) from continuing operations attributable to Key common shareholders assuming dilution			
	\$ .22	\$	.26
Income (loss) from discontinued operations, net of taxes (a)			.01
Net income (loss) attributable to Key common shareholders assuming dilution <sup>(d)</sup>	.22		.26

- (a) In September 2009, we decided to discontinue the education lending business conducted through Key Education Resources, the education payment and financing unit of KeyBank. As a result of this decision, we have accounted for this business as a discontinued operation. For further discussion regarding the income (loss) from discontinued operations, see Note 11 ( Acquisitions and Discontinued Operations ).
- (b) For the three months ended March 31, 2016, weighted-average common shares outstanding, effect of common share options and other stock awards, and weighted-average common shares and potential common shares outstanding have been revised from our financial results reported on Form 8-K on April 21, 2016.
- (c) Assumes conversion of common share options and other stock awards and/or convertible preferred stock, as applicable.
- (d) EPS may not foot due to rounding.

Table of Contents**3. Loans and Loans Held for Sale**

Our loans by category are summarized as follows:

<i>in millions</i>	<b>March 31, 2016</b>	<b>December 31, 2015</b>	<b>March 31, 2015</b>
Commercial, financial and agricultural <sup>(a)</sup>	<b>\$ 31,976</b>	\$ 31,240	\$ 28,783
Commercial real estate:			
Commercial mortgage	<b>8,364</b>	7,959	8,162
Construction	<b>841</b>	1,053	1,142
<b>Total commercial real estate loans</b>	<b>9,205</b>	9,012	9,304
Commercial lease financing <sup>(b)</sup>	<b>3,934</b>	4,020	4,064
<b>Total commercial loans</b>	<b>45,115</b>	44,272	42,151
Residential prime loans:			
Real estate residential mortgage	<b>2,234</b>	2,242	2,231
Home equity loans	<b>10,149</b>	10,335	10,523
<b>Total residential prime loans</b>	<b>12,383</b>	12,577	12,754
Consumer direct loans	<b>1,579</b>	1,600	1,547
Credit cards	<b>782</b>	806	727
Consumer indirect loans	<b>579</b>	621	774
<b>Total consumer loans</b>	<b>15,323</b>	15,604	15,802
<b>Total loans <sup>(c) (d)</sup></b>	<b>\$ 60,438</b>	\$ 59,876	\$ 57,953

- (a) Loan balances include \$85 million, \$85 million, and \$87 million of commercial credit card balances at March 31, 2016, December 31, 2015, and March 31, 2015, respectively.
- (b) Commercial lease financing includes receivables held as collateral for a secured borrowing of \$115 million, \$134 million, and \$230 million at March 31, 2016, December 31, 2015, and March 31, 2015, respectively. Principal reductions are based on the cash payments received from these related receivables. Additional information pertaining to this secured borrowing is included in Note 18 ( Long-Term Debt ) beginning on page 208 of our 2015 Form 10-K.
- (c) At March 31, 2016, total loans include purchased loans of \$109 million, of which \$11 million were PCI loans. At December 31, 2015, total loans include purchased loans of \$114 million, of which \$11 million were PCI loans. At March 31, 2015, total loans include purchased loans of \$130 million, of which \$12 million were PCI loans.
- (d) Total loans exclude loans of \$1.8 billion at March 31, 2016, \$1.8 billion at December 31, 2015, and \$2.2 billion at March 31, 2015, related to the discontinued operations of the education lending business. Additional information pertaining to these loans is provided in Note 11 ( Acquisitions and Discontinued Operations ).

Our loans held for sale are summarized as follows:

<i>in millions</i>	<b>March 31, 2016</b>	<b>December 31, 2015</b>	<b>March 31, 2015</b>
Commercial, financial and agricultural	\$ 103	\$ 76	\$ 183
Real estate commercial mortgage	562	532	1,408
Commercial lease financing		14	14
Real estate residential mortgage	19	17	44
<b>Total loans held for sale</b>	<b>\$ 684</b>	<b>\$ 639</b>	<b>\$ 1,649</b>

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Our quarterly summary of changes in loans held for sale follows:

<i>in millions</i>	<b>March 31, 2016</b>	<b>December 31, 2015</b>	<b>March 31, 2015</b>
Balance at beginning of the period	\$ 639	\$ 916	\$ 734
New originations	1,114	1,655	2,130
Transfers from (to) held to maturity, net		22	10
Loan sales	(1,108)	(1,943)	(1,204)
Loan draws (payments), net	39	(11)	(21)
Balance at end of period	\$ 684	\$ 639	\$ 1,649

Table of Contents**4. Asset Quality**

We assess the credit quality of the loan portfolio by monitoring net credit losses, levels of nonperforming assets and delinquencies, and credit quality ratings as defined by management.

Nonperforming loans are loans for which we do not accrue interest income, and include commercial and consumer loans and leases, as well as current year TDRs and nonaccruing TDR loans from prior years. Nonperforming loans do not include loans held for sale or PCI loans. Nonperforming assets include nonperforming loans, nonperforming loans held for sale, OREO, and other nonperforming assets.

Our nonperforming assets and past due loans were as follows:

<i>in millions</i>	<b>March 31, 2016</b>	<b>December 31, 2015</b>	<b>March 31, 2015</b>
Total nonperforming loans <sup>(a), (b)</sup>	\$ 676	\$ 387	\$ 437
OREO <sup>(c)</sup>	14	14	20
Other nonperforming assets	2	2	
Total nonperforming assets	\$ 692	\$ 403	\$ 457
Nonperforming assets from discontinued operations - education lending <sup>(d)</sup>	\$ 6	\$ 7	\$ 8
Restructured loans included in nonperforming loans	\$ 151	\$ 159	\$ 141
Restructured loans with an allocated specific allowance <sup>(e)</sup>	59	69	70
Specifically allocated allowance for restructured loans <sup>(f)</sup>	29	30	39
Accruing loans past due 90 days or more	\$ 70	\$ 72	\$ 111
Accruing loans past due 30 through 89 days	237	208	216

- (a) Loan balances exclude \$11 million, \$11 million, and \$12 million of PCI loans at March 31, 2016, December 31, 2015, and March 31, 2015, respectively.
- (b) Includes carrying value of consumer residential mortgage loans in the process of foreclosure of approximately \$131 million, \$114 million, and \$119 million at March 31, 2016, December 31, 2015, and March 31, 2015, respectively.
- (c) Includes carrying value of foreclosed residential real estate of approximately \$11 million, \$11 million, and \$17 million at March 31, 2016, December 31, 2015, and March 31, 2015, respectively.
- (d) Restructured loans of approximately \$21 million, \$21 million, and \$18 million are included in discontinued operations at March 31, 2016, December 31, 2015, and March 31, 2015, respectively. See Note 11 ( Acquisitions and Discontinued Operations ) for further discussion.
- (e) Included in individually impaired loans allocated a specific allowance.
- (f) Included in allowance for individually evaluated impaired loans.

We evaluate purchased loans for impairment in accordance with the applicable accounting guidance. Purchased loans that have evidence of deterioration in credit quality since origination and for which it is probable, at acquisition, that

all contractually required payments will not be collected are deemed PCI and initially recorded at fair value without recording an allowance for loan losses. All PCI loans were acquired in 2012. At the 2012 acquisition date, the estimated gross contractual amount receivable of all PCI loans totaled \$41 million. The estimated cash flows not expected to be collected (the nonaccretable amount) were \$11 million, and the accretable amount was approximately \$5 million. The difference between the fair value and the cash flows expected to be collected from the purchased loans is accreted to interest income over the remaining term of the loans.

At March 31, 2016, the outstanding unpaid principal balance and carrying value of all PCI loans was \$17 million and \$11 million, respectively, compared to \$17 million and \$11 million, respectively, at December 31, 2015, and \$19 million and \$12 million, respectively, at March 31, 2015. Changes in the accretable yield during the first quarter of 2016 included accretion and net reclassifications of less than \$1 million, resulting in an ending balance of \$5 million at March 31, 2016. Changes in the accretable yield during 2015 included accretion and net reclassifications of less than \$1 million, resulting in an ending balance of \$5 million at December 31, 2015, which was unchanged from the ending balance at December 31, 2014. Changes in the accretable yield during the first quarter of 2015 included accretion and net reclassifications of less than \$1 million, resulting in an ending balance of \$5 million at March 31, 2015.

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At March 31, 2016, the approximate carrying amount of our commercial nonperforming loans outstanding represented 89% of their original contractual amount owed, total nonperforming loans outstanding represented 88% of their original contractual amount owed, and nonperforming assets in total were carried at 88% of their original contractual amount owed.

At March 31, 2016, our 20 largest nonperforming loans totaled \$359 million, representing 54% of total loans on nonperforming status. At March 31, 2015, our 20 largest nonperforming loans totaled \$123 million, representing 28% of total loans on nonperforming status.

Nonperforming loans and loans held for sale reduced expected interest income by \$5 million for the three months ended March 31, 2016, and \$4 million for the three months ended March 31, 2015.

The following tables set forth a further breakdown of individually impaired loans as of March 31, 2016, December 31, 2015, and March 31, 2015:

<b>March 31, 2016</b> <i>in millions</i>	<b>Recorded Investment</b> <sup>(a)</sup>	<b>Unpaid Principal Balance</b> <sup>(b)</sup>	<b>Specific Allowance</b>	<b>Average Recorded Investment</b>
<b>With no related allowance recorded:</b>				
Commercial, financial and agricultural	\$ 260	\$ 270		\$ 150
<b>Commercial real estate:</b>				
Commercial mortgage	4	7		4
Construction	8	8		7
Total commercial real estate loans	12	15		11
<b>Total commercial loans</b>	<b>272</b>	<b>285</b>		<b>161</b>
Real estate residential mortgage	23	23		23
Home equity loans	68	68		65
Consumer indirect loans	1	1		1
<b>Total consumer loans</b>	<b>92</b>	<b>92</b>		<b>89</b>
Total loans with no related allowance recorded	364	377		250
<b>With an allowance recorded:</b>				
Commercial, financial and agricultural	101	113	\$ 28	64
<b>Commercial real estate:</b>				
Commercial mortgage	4	4	1	5
<b>Total commercial real estate loans</b>	<b>4</b>	<b>4</b>	<b>1</b>	<b>5</b>
Total commercial loans	105	117	29	69



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Real estate residential mortgage	32	32	3	33
Home equity loans	65	65	19	64
Consumer direct loans	3	3		3
Credit cards	3	3		3
Consumer indirect loans	35	35	3	36
Total consumer loans	138	138	25	139
Total loans with an allowance recorded	243	255	54	208
Total	\$ 607	\$ 632	\$ 54	\$ 458

- (a) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. This amount is a component of total loans on our consolidated balance sheet.
- (b) The Unpaid Principal Balance represents the customer's legal obligation to us.

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<b>December 31, 2015</b> <i>in millions</i>	<b>Recorded Investment <sup>(a)</sup></b>	<b>Unpaid Principal Balance <sup>(b)</sup></b>	<b>Specific Allowance</b>	<b>Average Recorded Investment</b>
<b>With no related allowance recorded:</b>				
Commercial, financial and agricultural	\$ 40	\$ 74		\$ 23
<b>Commercial real estate:</b>				
Commercial mortgage	5	8		10
Construction	5	5		5
Total commercial real estate loans	10	13		15
<b>Total commercial loans</b>	<b>50</b>	<b>87</b>		<b>38</b>
Real estate residential mortgage	23	23		24
Home equity loans	61	61		62
<b>Consumer direct loans</b>				
<b>Credit cards</b>				
Consumer indirect loans	1	1		1
<b>Total consumer loans</b>	<b>85</b>	<b>85</b>		<b>87</b>
Total loans with no related allowance recorded	135	172		125
<b>With an allowance recorded:</b>				
Commercial, financial and agricultural	28	43	\$ 7	33
<b>Commercial real estate:</b>				
Commercial mortgage	5	6	1	6
Construction				1
Total commercial real estate loans	5	6	1	7
<b>Total commercial loans</b>	<b>33</b>	<b>49</b>	<b>8</b>	<b>40</b>
Real estate residential mortgage	33	33	4	32
Home equity loans	64	64	20	60
Consumer direct loans	3	3		4
Credit cards	3	3		4
Consumer indirect loans	37	37	3	40
<b>Total consumer loans</b>	<b>140</b>	<b>140</b>	<b>27</b>	<b>140</b>
Total loans with an allowance recorded	173	189	35	180
<b>Total</b>	<b>\$ 308</b>	<b>\$ 361</b>	<b>\$ 35</b>	<b>\$ 305</b>

- (a) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. This amount is a component of total loans on our consolidated balance sheet.
- (b) The Unpaid Principal Balance represents the customer's legal obligation to us.

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<b>March 31, 2015</b> <i>in millions</i>	<b>Recorded Investment <sup>(a)</sup></b>	<b>Unpaid Principal Balance <sup>(b)</sup></b>	<b>Specific Allowance</b>	<b>Average Recorded Investment</b>
<b>With no related allowance recorded:</b>				
Commercial, financial and agricultural	\$ 20	\$ 51		\$ 13
<b>Commercial real estate:</b>				
Commercial mortgage	14	19		14
Construction	7	7		6
Total commercial real estate loans	21	26		20
<b>Total commercial loans</b>	<b>41</b>	<b>77</b>		<b>33</b>
Real estate residential mortgage	23	23		23
Home equity loans	63	64		63
Consumer indirect loans	1	1		2
<b>Total consumer loans</b>	<b>87</b>	<b>88</b>		<b>88</b>
Total loans with no related allowance recorded	128	165		121
<b>With an allowance recorded:</b>				
Commercial, financial and agricultural	62	62	\$ 20	50
<b>Commercial real estate:</b>				
Commercial mortgage	6	7	2	6
Construction				1
Total commercial real estate loans	6	7	2	7
<b>Total commercial loans</b>	<b>68</b>	<b>69</b>	<b>22</b>	<b>57</b>
Real estate residential mortgage	32	32	5	32
Home equity loans	60	60	18	59
Consumer direct loans	3	3		3
Credit cards	4	4		4
Consumer indirect loans	43	43	4	44
<b>Total consumer loans</b>	<b>142</b>	<b>142</b>	<b>27</b>	<b>142</b>
Total loans with an allowance recorded	210	211	49	199
<b>Total</b>	<b>\$ 338</b>	<b>\$ 376</b>	<b>\$ 49</b>	<b>\$ 320</b>

(a) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct

charge-offs. This amount is a component of total loans on our consolidated balance sheet.

(b) The Unpaid Principal Balance represents the customer's legal obligation to us.

For the three months ended March 31, 2016, and March 31, 2015, interest income recognized on the outstanding balances of accruing impaired loans totaled \$4 million and \$1 million, respectively.

At March 31, 2016, aggregate restructured loans (accrual and nonaccrual loans) totaled \$283 million, compared to \$280 million at December 31, 2015, and \$268 million at March 31, 2015. During the first three months of 2016, we added \$23 million in restructured loans, which were partially offset by \$20 million in payments and charge-offs. During 2015, we added \$99 million in restructured loans, which were partially offset by \$89 million in payments and charge-offs. During the first three months of 2015, we added \$11 million in restructured loans, which were offset by \$13 million in payments and charge-offs.

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A further breakdown of TDRs included in nonperforming loans by loan category as of March 31, 2016, follows:

<b>March 31, 2016</b> <i>dollars in millions</i>	<b>Number of Loans</b>	<b>Pre-modification Outstanding Recorded Investment</b>	<b>Post-modification Outstanding Recorded Investment</b>
<b>LOAN TYPE</b>			
<b>Nonperforming:</b>			
Commercial, financial and agricultural	13	\$ 58	\$ 46
Commercial real estate:			
Real estate commercial mortgage	10	13	4
Total commercial loans	23	71	50
Real estate residential mortgage	323	21	21
Home equity loans	1,350	85	76
Consumer direct loans	29	1	
Credit cards	253	1	1
Consumer indirect loans	94	4	3
Total consumer loans	2,049	112	101
<b>Total nonperforming TDRs</b>	<b>2,072</b>	<b>183</b>	<b>151</b>
<b>Prior-year accruing: <sup>(a)</sup></b>			
Commercial, financial and agricultural	7	5	2
Total commercial loans	7	5	2
Real estate residential mortgage	532	36	36
Home equity loans	1,149	68	57
Consumer direct loans	41	2	2
Credit cards	488	3	2
Consumer indirect loans	445	59	33
Total consumer loans	2,655	168	130
<b>Total prior-year accruing TDRs</b>	<b>2,662</b>	<b>173</b>	<b>132</b>
<b>Total TDRs</b>	<b>4,734</b>	<b>\$ 356</b>	<b>\$ 283</b>

(a) All TDRs that were restructured prior to January 1, 2016, and are fully accruing.

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A further breakdown of TDRs included in nonperforming loans by loan category as of December 31, 2015, follows:

<b>December 31, 2015</b> <i>dollars in millions</i>	<b>Number of Loans</b>	<b>Pre-modification Outstanding Recorded Investment</b>	<b>Post-modification Outstanding Recorded Investment</b>
<b>LOAN TYPE</b>			
<b>Nonperforming:</b>			
Commercial, financial and agricultural	12	\$ 56	\$ 45
Commercial real estate:			
Real estate commercial mortgage	12	30	7
Total commercial real estate loans	12	30	7
Total commercial loans	24	86	52
Real estate residential mortgage	366	23	23
Home equity loans	1,262	85	76
Consumer direct loans	28	1	1
Credit cards	339	2	2
Consumer indirect loans	103	6	5
Total consumer loans	2,098	117	107
Total nonperforming TDRs	2,122	203	159
<b>Prior-year accruing: <sup>(a)</sup></b>			
Commercial, financial and agricultural	7	5	2
Commercial real estate:			
Real estate commercial mortgage			
Total commercial real estate loans			
Total commercial loans	7	5	2
Real estate residential mortgage	489	34	34
Home equity loans	1,071	57	49
Consumer direct loans	42	2	2
Credit cards	461	4	2
Consumer indirect loans	430	59	32
Total consumer loans	2,493	156	119
Total prior-year accruing TDRs	2,500	161	121
Total TDRs	4,622	\$ 364	\$ 280

- (a) All TDRs that were restructured prior to January 1, 2015, and are fully accruing.



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A further breakdown of TDRs included in nonperforming loans by loan category as of March 31, 2015, follows:

<b>March 31, 2015</b> <i>dollars in millions</i>	<b>Number of Loans</b>	<b>Pre-modification Outstanding Recorded Investment</b>	<b>Post-modification Outstanding Recorded Investment</b>
<b>LOAN TYPE</b>			
<b>Nonperforming:</b>			
Commercial, financial and agricultural	11	\$ 25	\$ 22
Commercial real estate:			
Real estate commercial mortgage	12	37	13
Total commercial real estate loans	12	37	13
Total commercial loans	23	62	35
Real estate residential mortgage	383	22	22
Home equity loans	1,199	80	73
Consumer direct loans	28	1	1
Credit cards	275	2	1
Consumer indirect loans	143	9	9
Total consumer loans	2,028	114	106
Total nonperforming TDRs	2,051	176	141
<b>Prior-year accruing: <sup>(a)</sup></b>			
Commercial, financial and agricultural	17	6	3
Commercial real estate:			
Real estate commercial mortgage	1	2	1
Total commercial real estate loans	1	2	1
Total commercial loans	18	8	4
Real estate residential mortgage	454	34	34
Home equity loans	1,142	57	49
Consumer direct loans	51	2	2
Credit cards	519	4	2
Consumer indirect loans	505	62	36
Total consumer loans	2,671	159	123
Total prior-year accruing TDRs	2,689	167	127
Total TDRs	4,740	\$ 343	\$ 268

(a) All TDRs that were restructured prior to January 1, 2015, and are fully accruing.

We classify loan modifications as TDRs when a borrower is experiencing financial difficulties and we have granted a concession without commensurate financial, structural, or legal consideration. All commercial and consumer loan TDRs, regardless of size, are individually evaluated for impairment to determine the probable loss content and are assigned a specific loan allowance if deemed appropriate. This designation has the effect of moving the loan from the general reserve methodology (i.e., collectively evaluated) to the specific reserve methodology (i.e., individually evaluated) and may impact the ALLL through a charge-off or increased loan loss provision. These components affect the ultimate allowance level. Additional information regarding TDRs for discontinued operations is provided in Note 11 ( Acquisitions and Discontinued Operations ).

Commercial loan TDRs are considered defaulted when principal and interest payments are 90 days past due. Consumer loan TDRs are considered defaulted when principal and interest payments are more than 60 days past due. During the first three months of 2016, there were no commercial loan TDRs and 51 consumer loan TDRs with a combined recorded investment of \$3 million that experienced payment defaults after modifications resulting in TDR status during 2015. During the first three months of 2015, there were no significant commercial loan TDRs and 89 consumer loan TDRs with a combined recorded investment of \$4 million that experienced payment defaults from modifications resulting in TDR status during 2014. As TDRs are individually evaluated for impairment under the specific reserve methodology, subsequent defaults do not generally have a significant additional impact on the ALLL.

Our loan modifications are handled on a case-by-case basis and are negotiated to achieve mutually agreeable terms that maximize loan collectability and meet the borrower's financial needs. Our concession types are primarily interest rate reductions, forgiveness of principal, and other modifications. The commercial TDR other concession category includes modification of loan terms, covenants, or conditions. The consumer TDR other concession category primarily includes those borrowers' debts that are discharged through Chapter 7 bankruptcy and have not been formally re-affirmed.

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The following table shows the post-modification outstanding recorded investment by concession type for our commercial and consumer accruing and nonaccruing TDRs and other selected financial data.

<i>in millions</i>	March 31, 2016	December 31, 2015	March 31, 2015
<b>Commercial loans:</b>			
Interest rate reduction	\$ 48	\$ 51	\$ 12
Forgiveness of principal		2	2
Other	4	1	25
<b>Total</b>	<b>\$ 52</b>	<b>\$ 54</b>	<b>\$ 39</b>
<b>Consumer loans:</b>			
Interest rate reduction	\$ 128	\$ 132	\$ 140
Forgiveness of principal	20	8	4
Other	83	86	85
<b>Total</b>	<b>\$ 231</b>	<b>\$ 226</b>	<b>\$ 229</b>
<b>Total commercial and consumer TDRs <sup>(a)</sup></b>	<b>\$ 283</b>	<b>\$ 280</b>	<b>\$ 268</b>
<b>Total loans</b>	<b>60,438</b>	<b>59,876</b>	<b>57,953</b>

(a) Commitments outstanding to lend additional funds to borrowers whose loan terms have been modified in TDRs are \$6 million, \$9 million, and \$5 million at March 31, 2016, December 31, 2015, and March 31, 2015, respectively.

Our policies for determining past due loans, placing loans on nonaccrual, applying payments on nonaccrual loans, and resuming accrual of interest for our commercial and consumer loan portfolios are disclosed in Note 1 ( Summary of Significant Accounting Policies ) under the heading Nonperforming Loans beginning on page 121 of our 2015 Form 10-K.

At March 31, 2016, approximately \$59.4 billion, or 98.4%, of our total loans were current, compared to approximately \$59.2 billion, or 98.9% of total loans, at December 31, 2015, and approximately \$57.2 billion, or 98.7% of total loans, at March 31, 2015. At March 31, 2016, total past due loans and nonperforming loans of \$983 million represented approximately 1.6% of total loans, compared to \$667 million, or 1.1% of total loans, at December 31, 2015, and \$764 million, or 1.3% of total loans, at March 31, 2015.

The following aging analysis of past due and current loans as of March 31, 2016, December 31, 2015, and March 31, 2015, provides further information regarding Key's credit exposure.

	30-59	60-89	90 and Greater	Total Past Due and Purchased
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<b>March 31, 2016</b> <i>in millions</i>	<b>Current</b>	<b>Days Past Due</b>	<b>Days Past Due</b>	<b>Days Past Due</b>	<b>Nonperforming Loans</b>	<b>Nonperforming Loans</b>	<b>Credit Impaired</b>	<b>Total Loans</b>
<b>LOAN TYPE</b>								
Commercial, financial and agricultural	\$ 31,522	\$ 30	\$ 31	\$ 13	\$ 380	\$ 454		\$ 31,976
Commercial real estate:								
Commercial mortgage	8,327	3	3	15	16	37		8,364
Construction	807	20	1	1	12	34		841
Total commercial real estate loans	9,134	23	4	16	28	71		9,205
Commercial lease financing	3,868	18	25	12	11	66		3,934
Total commercial loans	\$ 44,524	\$ 71	\$ 60	\$ 41	\$ 419	\$ 591		\$ 45,115
Real estate residential mortgage	\$ 2,151	\$ 10	\$ 2	\$ 2	\$ 59	\$ 73	\$ 10	\$ 2,234
Home equity loans	9,879	45	20	13	191	269	1	10,149
Consumer direct loans	1,564	6	3	5	1	15		1,579
Credit cards	764	5	4	7	2	18		782
Consumer indirect loans	562	9	2	2	4	17		579
Total consumer loans	\$ 14,920	\$ 75	\$ 31	\$ 29	\$ 257	\$ 392	\$ 11	\$ 15,323
Total loans	\$ 59,444	\$ 146	\$ 91	\$ 70	\$ 676	\$ 983	\$ 11	\$ 60,438

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December 31, 2015 <i>in millions</i>	30-59 Days Past Due			90 and Greater Days Past Due		Nonperforming Loans	Nonperforming Loans	Credit Impaired	Total Past Due and Purchased Loans
	Current	Due	Due	Due	Due				
<b>LOAN TYPE</b>									
Commercial, financial and agricultural	\$ 31,116	\$ 11	\$ 11	\$ 20	\$ 82	\$ 124			\$ 31,240
Commercial real estate:									
Commercial mortgage	7,917	8	5	10	19	42			7,959
Construction	1,042	1	1		9	11			1,053
Total commercial real estate loans	8,959	9	6	10	28	53			9,012
Commercial lease financing	3,952	33	11	11	13	68			4,020
Total commercial loans	\$ 44,027	\$ 53	\$ 28	\$ 41	\$ 123	\$ 245			\$ 44,272
Real estate residential mortgage	\$ 2,149	\$ 14	\$ 3	\$ 2	\$ 64	\$ 83	\$ 10		\$ 2,242
Home equity loans	10,056	50	24	14	190	278	1		10,335
Consumer direct loans	1,580	10	3	5	2	20			1,600
Credit cards	785	6	4	9	2	21			806
Consumer indirect loans	601	9	4	1	6	20			621
Total consumer loans	\$ 15,171	\$ 89	\$ 38	\$ 31	\$ 264	\$ 422	\$ 11		\$ 15,604
Total loans	\$ 59,198	\$ 142	\$ 66	\$ 72	\$ 387	\$ 667	\$ 11		\$ 59,876

March 31, 2015 <i>in millions</i>	30-59 Days Past Due			90 and Greater Days Past Due		Nonperforming Loans	Nonperforming Loans	Credit Impaired	Total Past Due and Purchased Loans
	Current	Due	Due	Due	Due				
<b>LOAN TYPE</b>									
Commercial, financial and agricultural	\$ 28,603	\$ 36	\$ 11	\$ 35	\$ 98	\$ 180			\$ 28,783
Commercial real estate:									
Commercial mortgage	8,080	5	18	29	30	82			8,162
Construction	1,114	10	4	2	12	28			1,142
Total commercial real estate loans	9,194	15	22	31	42	110			9,304
Commercial lease financing	4,017	9	6	12	20	47			4,064
Total commercial loans	\$ 41,814	\$ 60	\$ 39	\$ 78	\$ 160	\$ 337			\$ 42,151

Real estate residential mortgage	\$ 2,129	\$ 12	\$ 5	\$ 2	\$ 72	\$ 91	\$ 11	\$ 2,231
Home equity loans	10,250	43	24	14	191	272	1	10,523
Consumer direct loans	1,527	8	4	6	2	20		1,547
Credit cards	708	5	3	9	2	19		727
Consumer indirect loans	749	9	4	2	10	25		774
Total consumer loans	\$ 15,363	\$ 77	\$ 40	\$ 33	\$ 277	\$ 427	\$ 12	\$ 15,802
Total loans	\$ 57,177	\$ 137	\$ 79	\$ 111	\$ 437	\$ 764	\$ 12	\$ 57,953

The prevalent risk characteristic for both commercial and consumer loans is the risk of loss arising from an obligor's inability or failure to meet contractual payment or performance terms. Evaluation of this risk is stratified and monitored by the loan risk rating grades assigned for the commercial loan portfolios and the regulatory risk ratings assigned for the consumer loan portfolios.

Most extensions of credit are subject to loan grading or scoring. Loan grades are assigned at the time of origination, verified by credit risk management, and periodically re-evaluated thereafter. This risk rating methodology blends our judgment with quantitative modeling. Commercial loans generally are assigned two internal risk ratings. The first rating reflects the probability that the borrower will default on an obligation; the second rating reflects expected recovery rates on the credit facility. Default probability is determined based on, among other factors, the financial strength of the borrower, an assessment of the borrower's management, the borrower's competitive position within its industry sector, and our view of industry risk in the context of the general economic outlook. Types of exposure, transaction structure, and collateral, including credit risk mitigants, affect the expected recovery assessment.

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Credit quality indicators for our commercial and consumer loan portfolios, excluding \$11 million and \$12 million of PCI loans at March 31, 2016, and March 31, 2015, respectively, based on regulatory classification and payment activity as of March 31, 2016, and March 31, 2015, are as follows:

**Commercial Credit Exposure****Credit Risk Profile by Creditworthiness Category** <sup>(a)</sup> <sup>(b)</sup>

<i>in millions</i>	Commercial, financial and agricultural			RE Commercial		RE Construction			
	March 31, 2016	December 31, 2015	March 31, 2015	March 31, 2016	December 31, 2015	March 31, 2015	December 2015	March 31, 2015	
<b>RATING</b>									
Pass	\$ 30,335	\$ 29,921	\$ 27,886	\$ 8,176	\$ 7,800	\$ 7,937	\$ 796	\$ 1,007	\$ 1,120
Criticized (Accruing)	1,260	1,236	798	172	139	195	33	37	10
Criticized (Nonaccruing)	381	83	99	16	20	30	12	9	12
Total	\$ 31,976	\$ 31,240	\$ 28,783	\$ 8,364	\$ 7,959	\$ 8,162	\$ 841	\$ 1,053	\$ 1,142

<b>RATING</b>	Commercial Lease			Total		
	March 31, 2016	December 31, 2015	March 31, 2015	March 31, 2016	December 31, 2015	March 31, 2015
Pass	\$ 3,878	\$ 3,967	\$ 3,996	\$ 43,185	\$ 42,695	\$ 40,939
Criticized (Accruing)	45	38	48	1,510	1,450	1,051
Criticized (Nonaccruing)	11	15	20	420	127	161
Total	\$ 3,934	\$ 4,020	\$ 4,064	\$ 45,115	\$ 44,272	\$ 42,151

- (a) Credit quality indicators are updated on an ongoing basis and reflect credit quality information as of the dates indicated.
- (b) The term criticized refers to those loans that are internally classified by Key as special mention or worse, which are asset quality categories defined by regulatory authorities. These assets have an elevated level of risk and may have a high probability of default or total loss. Pass rated refers to all loans not classified as criticized.

**Consumer Credit Exposure****Credit Risk Profile by Regulatory Classifications** <sup>(a)</sup> <sup>(b)</sup>

**Residential Prime**

GRADE	March	December 31, 2015	March 31, 2015
	31, 2016		
Pass	\$ 12,107	\$ 12,296	\$ 12,463
Substandard	265	270	279
<b>Total</b>	<b>\$ 12,372</b>	<b>\$ 12,566</b>	<b>\$ 12,742</b>

#### Credit Risk Profile Based on Payment Activity (a)

<i>in millions</i>	Consumer direct loans			Credit cards			Consumer indirect loans		
	March 31, 2016	December 31, 2015	March 31, 2015	March 31, 2016	December 31, 2015	March 31, 2015	March 31, 2016	December 31, 2015	March 31, 2015
	Performing	\$ 1,578	\$ 1,598	\$ 1,545	\$ 780	\$ 804	\$ 725	\$ 575	\$ 615
Nonperforming	1	2	2	2	2	2	4	6	10
<b>Total</b>	<b>\$ 1,579</b>	<b>\$ 1,600</b>	<b>\$ 1,547</b>	<b>\$ 782</b>	<b>\$ 806</b>	<b>\$ 727</b>	<b>\$ 579</b>	<b>\$ 621</b>	<b>\$ 774</b>

	March 31, 2016	Total December 31, 2015	March 31, 2015
	Performing	\$ 2,933	\$ 3,017
Nonperforming	7	10	14
<b>Total</b>	<b>\$ 2,940</b>	<b>\$ 3,027</b>	<b>\$ 3,048</b>

- (a) Credit quality indicators are updated on an ongoing basis and reflect credit quality information as of the dates indicated.
- (b) Our past due payment activity to regulatory classification conversion is as follows: pass = less than 90 days; and substandard = 90 days and greater plus nonperforming loans.

We determine the appropriate level of the ALLL on at least a quarterly basis. The methodology is described in Note 1 ( Summary of Significant Accounting Policies ) under the heading Allowance for Loan and Lease Losses beginning on page 122 of our 2015 Form 10-K. We apply expected loss rates to existing loans with similar risk characteristics as noted in the credit quality indicator table above and exercise judgment to assess the impact of qualitative factors such as changes in economic conditions, changes in credit policies or underwriting standards, and changes in the level of credit risk associated with specific industries and markets.

For all commercial and consumer loan TDRs, regardless of size, as well as impaired commercial loans with an outstanding balance of \$2.5 million or greater, we conduct further analysis to determine the probable loss content and assign a specific



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allowance to the loan if deemed appropriate. We estimate the extent of the individual impairment for commercial loans and TDRs by comparing the recorded investment of the loan with the estimated present value of its future cash flows, the fair value of its underlying collateral, or the loan's observable market price. Secured consumer loan TDRs that are discharged through Chapter 7 bankruptcy and not formally re-affirmed are adjusted to reflect the fair value of the underlying collateral, less costs to sell. Non-Chapter 7 consumer loan TDRs are combined in homogenous pools and assigned a specific allocation based on the estimated present value of future cash flows using the loan's effective interest rate. A specific allowance also may be assigned even when sources of repayment appear sufficient if we remain uncertain about whether the loan will be repaid in full. On at least a quarterly basis, we evaluate the appropriateness of our loss estimation methods to reduce differences between estimated incurred losses and actual losses. The ALLL at March 31, 2016, represents our best estimate of the probable credit losses inherent in the loan portfolio at that date.

Commercial loans generally are charged off in full or charged down to the fair value of the underlying collateral when the borrower's payment is 180 days past due. Consumer loans generally are charged off when payments are 120 days past due. Home equity and residential mortgage loans generally are charged down to net realizable value when payment is 180 days past due. Credit card loans, and similar unsecured products, are charged off when payments are 180 days past due.

At March 31, 2016, the ALLL was \$826 million, or 1.37% of loans, compared to \$794 million, or 1.37% of loans, at March 31, 2015. At March 31, 2016, the ALLL was 122.2% of nonperforming loans, compared to 181.7% at March 31, 2015.

A summary of the changes in the ALLL for the periods indicated is presented in the table below:

<i>in millions</i>	<b>Three months ended March 31,</b>	
	<b>2016</b>	<b>2015</b>
Balance at beginning of period continuing operations	\$ 796	\$ 794
Charge-offs	(60)	(47)
Recoveries	14	19
Net loans and leases charged off	(46)	(28)
Provision for loan and lease losses from continuing operations	76	29
Foreign currency translation adjustment		(1)
Balance at end of period continuing operations	\$ 826	\$ 794

The changes in the ALLL by loan category for the periods indicated are as follows:

<i>in millions</i>	<b>December 31,</b>				<b>March 31,</b>
	<b>2015</b>	<b>Provision</b>	<b>Charge-offs</b>	<b>Recoveries</b>	<b>2016</b>
Commercial, financial and agricultural	\$ 450	\$ 50	\$ (26)	\$ 3	\$ 477
Real estate commercial mortgage	134		(1)	2	135

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Real estate construction	25	(3)		1	23
Commercial lease financing	47	(1)	(3)		43
<b>Total commercial loans</b>	<b>656</b>	<b>46</b>	<b>(30)</b>	<b>6</b>	<b>678</b>
Real estate residential mortgage	18	2	(2)	2	20
Home equity loans	57	14	(10)	3	64
Consumer direct loans	20	5	(6)	1	20
Credit cards	32	6	(8)	1	31
Consumer indirect loans	13	3	(4)	1	13
<b>Total consumer loans</b>	<b>140</b>	<b>30</b>	<b>(30)</b>	<b>8</b>	<b>148</b>
<b>Total ALLL continuing operations</b>	<b>796</b>	<b>76<sup>(a)</sup></b>	<b>(60)</b>	<b>14</b>	<b>826</b>
Discontinued operations	28	2	(9)	3	24
<b>Total ALLL including discontinued operations</b>	<b>\$ 824</b>	<b>\$ 78</b>	<b>\$ (69)</b>	<b>\$ 17</b>	<b>\$ 850</b>

(a) Excludes a provision for losses on lending-related commitments of \$13 million.

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<i>in millions</i>	December 31,			March 31,		
	2014	Provision	Charge-offs	Recoveries	2015	
Commercial, financial and agricultural	\$ 391	\$ 21	\$ (12)	\$ 5	\$ 405	
Real estate commercial mortgage	148		(2)	2	148	
Real estate construction	28	1	(1)		28	
Commercial lease financing	56	(3)	(2)	4	55	
<b>Total commercial loans</b>	<b>623</b>	<b>19</b>	<b>(17)</b>	<b>11</b>	<b>636</b>	
Real estate residential mortgage	23		(2)		21	
Home equity loans	71	(3)	(8)	3	63	
Consumer direct loans	22	3	(6)	2	21	
Credit cards	33	7	(8)		32	
Consumer indirect loans	22	2	(6)	3	21	
<b>Total consumer loans</b>	<b>171</b>	<b>9</b>	<b>(30)</b>	<b>8</b>	<b>158</b>	
<b>Total ALLL continuing operations</b>	<b>794</b>	<b>28<sup>(a)</sup></b>	<b>(47)</b>	<b>19</b>	<b>794</b>	
Discontinued operations	29	2	(10)	4	25	
<b>Total ALLL including discontinued operations</b>	<b>\$ 823</b>	<b>\$ 30</b>	<b>\$ (57)</b>	<b>\$ 23</b>	<b>\$ 819</b>	

(a) Includes a \$1 million foreign currency translation adjustment. Excludes provision for losses on lending-related commitments of \$6 million.

Our ALLL from continuing operations increased by \$32 million, or 4%, from the first quarter of 2015. Our allowance applies expected loss rates to our existing loans with similar risk characteristics as well as any adjustments to reflect our current assessment of qualitative factors, such as changes in economic conditions, underwriting standards, and concentrations of credit. Our commercial ALLL increased by \$42 million, or 6.6%, from the first quarter of 2015 primarily because of loan growth and increased incurred loss estimates. The increase in these incurred loss estimates during 2015 was primarily due to the continued decline in oil and gas prices since 2014. Partially offsetting this increase was a decrease in our consumer ALLL of \$10 million, or 6.3%, from the first quarter of 2015. Our consumer ALLL decrease was primarily due to continued improvement in credit metrics, such as delinquency, average credit bureau score, and loan to value, which have decreased expected loss rates since 2014. The continued improvement in the consumer portfolio credit quality metrics from the first quarter of 2015 was primarily due to continued improved credit quality and benefits of relatively stable economic conditions.

For continuing operations, the loans outstanding individually evaluated for impairment totaled \$607 million, with a corresponding allowance of \$54 million at March 31, 2016. Loans outstanding collectively evaluated for impairment totaled \$59.8 billion, with a corresponding allowance of \$771 million at March 31, 2016. At March 31, 2016, PCI loans evaluated for impairment totaled \$11 million, with a corresponding allowance of \$1 million. There was no provision for loan and lease losses on these PCI loans during the quarter ended March 31, 2016. At March 31, 2015, the loans outstanding individually evaluated for impairment totaled \$338 million, with a corresponding allowance of \$49 million. Loans outstanding collectively evaluated for impairment totaled \$57.6 billion, with a corresponding allowance of \$744 million at March 31, 2015. At March 31, 2015, PCI loans evaluated for impairment totaled \$12 million, with a corresponding allowance of \$1 million. There was no provision for loan and lease losses on these PCI loans during the quarter ended March 31, 2015.



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A breakdown of the individual and collective ALLL and the corresponding loan balances as of March 31, 2016, follows:

March 31, 2016 <i>in millions</i>	Allowance			Loans	Outstanding		Purchased Credit Impaired
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Purchased Credit Impaired		Individually Evaluated for Impairment	Collectively Evaluated for Impairment	
Commercial, financial and agricultural	\$ 28	\$ 449		\$ 31,976	\$ 361	\$ 31,615	
Commercial real estate:							
Commercial mortgage	1	134		8,364	8	8,356	
Construction		23		841	8	833	
Total commercial real estate loans	1	157		9,205	16	9,189	
Commercial lease financing		43		3,934		3,934	
Total commercial loans	29	649		45,115	377	44,738	
Real estate residential mortgage	3	16	\$ 1	2,234	55	2,169	\$ 10
Home equity loans	19	45		10,149	133	10,015	1
Consumer direct loans		20		1,579	3	1,576	
Credit cards		31		782	3	779	
Consumer indirect loans	3	10		579	36	543	
Total consumer loans	25	122	1	15,323	230	15,082	11
Total ALLL continuing operations	54	771	1	60,438	607	59,820	11
Discontinued operations	2	22		1,760(a)	21	1,739(a)	
Total ALLL including discontinued operations	\$ 56	\$ 793	\$ 1	\$ 62,198	\$ 628	\$ 61,559	\$ 11

(a) Amount includes \$3 million of loans carried at fair value that are excluded from ALLL consideration.

A breakdown of the individual and collective ALLL and the corresponding loan balances as of December 31, 2015, follows:

December 31, 2015 <i>in millions</i>	Allowance			Loans	Outstanding		Purchased Credit Impaired
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Purchased Credit Impaired		Individually Evaluated for Impairment	Collectively Evaluated for Impairment	

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Commercial, financial and agricultural	\$ 7	\$ 443		\$ 31,240	\$ 68	\$ 31,172	
Commercial real estate:							
Commercial mortgage	1	133		7,959	10	7,949	
Construction		25		1,053	5	1,048	
Total commercial real estate loans	1	158		9,012	15	8,997	
Commercial lease financing		47		4,020		4,020	
Total commercial loans	8	648		44,272	83	44,189	
Real estate residential mortgage	4	13	\$ 1	2,242	56	2,176	\$ 10
Home equity loans	20	37		10,335	125	10,209	1
Consumer direct loans		20		1,600	3	1,597	
Credit cards		32		806	3	803	
Consumer indirect loans	3	10		621	38	583	
Total consumer loans	27	112	1	15,604	225	15,368	11
Total ALLL continuing operations	35	760	1	59,876	308	59,557	11
Discontinued operations	2	26		1,828(a)	21	1,807(a)	
Total ALLL including discontinued operations	\$ 37	\$ 786	\$ 1	\$ 61,704	\$ 329	\$ 61,364	\$ 11

(a) Amount includes \$4 million of loans carried at fair value that are excluded from ALLL consideration.

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A breakdown of the individual and collective ALLL and the corresponding loan balances as of March 31, 2015, follows:

March 31, 2015 <i>in millions</i>	Allowance			Loans	Outstanding		Purchased Credit Impaired
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Purchased Credit Impaired		Individually Evaluated for Impairment	Collectively Evaluated for Impairment	
Commercial, financial and agricultural	\$ 20	\$ 385		\$ 28,783	\$ 82	\$ 28,701	
Commercial real estate:							
Commercial mortgage	2	146		8,162	20	8,142	
Construction		28		1,142	7	1,135	
Total commercial real estate loans	2	174		9,304	27	9,277	
Commercial lease financing		55		4,064		4,064	
Total commercial loans	22	614		42,151	109	42,042	
Real estate residential mortgage	5	15	\$ 1	2,231	55	2,165	\$ 11
Home equity loans	18	45		10,523	123	10,399	1
Consumer direct loans		21		1,547	3	1,544	
Credit cards		32		727	4	723	
Consumer indirect loans	4	17		774	44	730	
Total consumer loans	27	130	1	15,802	229	15,561	12
Total ALLL continuing operations	49	744	1	57,953	338	57,603	12
Discontinued operations	1	24		2,219 <sup>(a)</sup>	18	2,201 <sup>(a)</sup>	
Total ALLL including discontinued operations	\$ 50	\$ 768	\$ 1	\$ 60,172	\$ 356	\$ 59,804	\$ 12

(a) Amount includes \$187 million of loans carried at fair value that are excluded from ALLL consideration. The liability for credit losses inherent in lending-related unfunded commitments, such as letters of credit and unfunded loan commitments, is included in accrued expense and other liabilities on the balance sheet. We establish the amount of this reserve by considering both historical trends and current market conditions quarterly, or more often if deemed necessary. Our liability for credit losses on lending-related commitments was \$69 million at March 31, 2016. When combined with our ALLL, our total allowance for credit losses represented 1.48% of loans at March 31, 2016, compared to 1.44% at March 31, 2015.

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

<i>in millions</i>	<b>Three months ended March 31,</b>	
	<b>2016</b>	<b>2015</b>
Balance at beginning of period	\$ 56	\$ 35
Provision (credit) for losses on lending-related commitments	13	6
Balance at end of period	\$ 69	\$ 41



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**5. Fair Value Measurements**

**Fair Value Determination**

As defined in the applicable accounting guidance, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in our principal market. We have established and documented our process for determining the fair values of our assets and liabilities, where applicable. Fair value is based on quoted market prices, when available, for identical or similar assets or liabilities. In the absence of quoted market prices, we determine the fair value of our assets and liabilities using valuation models or third-party pricing services. Both of these approaches rely on market-based parameters, when available, such as interest rate yield curves, option volatilities, and credit spreads, or unobservable inputs. Unobservable inputs may be based on our judgment, assumptions, and estimates related to credit quality, liquidity, interest rates, and other relevant inputs.

Valuation adjustments, such as those pertaining to counterparty and our own credit quality and liquidity, may be necessary to ensure that assets and liabilities are recorded at fair value. Credit valuation adjustments are made when market pricing does not accurately reflect the counterparty's or our own credit quality. We make liquidity valuation adjustments to the fair value of certain assets to reflect the uncertainty in the pricing and trading of the instruments when we are unable to observe recent market transactions for identical or similar instruments. Liquidity valuation adjustments are based on the following factors:

the amount of time since the last relevant valuation;

whether there is an actual trade or relevant external quote available at the measurement date; and

volatility associated with the primary pricing components.

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

an independent review and approval of valuation models and assumptions;

recurring detailed reviews of profit and loss; and

a validation of valuation model components against benchmark data and similar products, where possible. We recognize transfers between levels of the fair value hierarchy at the end of the reporting period. Quarterly, we review any changes to our valuation methodologies to ensure they are appropriate and justified, and refine our valuation methodologies if more market-based data becomes available. The Fair Value Committee, which is governed by ALCO, oversees the valuation process. Various Working Groups that report to the Fair Value Committee analyze and approve the underlying assumptions and valuation adjustments. Changes in valuation methodologies for Level 1 and Level 2 instruments are presented to the Accounting Policy group for approval. Changes in valuation methodologies for Level 3 instruments are presented to the Fair Value Committee for approval. The Working Groups are discussed in more detail in the qualitative disclosures within this note and in Note 11 ( Acquisitions and

Discontinued Operations ). Formal documentation of the fair valuation methodologies is prepared by the lines of business and support areas as appropriate. The documentation details the asset or liability class and related general ledger accounts, valuation techniques, fair value hierarchy level, market participants, accounting methods, valuation methodology, group responsible for valuations, and valuation inputs.

Additional information regarding our accounting policies for determining fair value is provided in Note 1 ( Summary of Significant Accounting Policies ) under the heading Fair Value Measurements beginning on page 124 of our 2015 Form 10-K.

### **Qualitative Disclosures of Valuation Techniques**

**Loans.** Most loans recorded as trading account assets are valued based on market spreads for similar assets since they are actively traded. Therefore, these loans are classified as Level 2 because the fair value recorded is based on observable market data for similar assets.

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*Securities (trading and available for sale).* We own several types of securities, requiring a range of valuation methods:

Securities are classified as Level 1 when quoted market prices are available in an active market for the identical securities. Level 1 instruments include exchange-traded equity securities.

Securities are classified as Level 2 if quoted prices for identical securities are not available, and fair value is determined using pricing models (either by a third-party pricing service or internally) or quoted prices of similar securities. These instruments include municipal bonds; bonds backed by the U.S. government; corporate bonds; certain mortgage-backed securities; securities issued by the U.S. Treasury; money markets; and certain agency and corporate CMOs. Inputs to the pricing models include: standard inputs, such as yields, benchmark securities, bids, and offers; actual trade data (i.e., spreads, credit ratings, and interest rates) for comparable assets; spread tables; matrices; high-grade scales; and option-adjusted spreads.

Securities are classified as Level 3 when there is limited activity in the market for a particular instrument. To determine fair value in such cases, depending on the complexity of the valuations required, we use internal models based on certain assumptions or a third-party valuation service. At March 31, 2016, our Level 3 instruments consist of two convertible preferred securities. Our Strategy group is responsible for reviewing the valuation model and determining the fair value of these investments on a quarterly basis. The securities are valued using a cash flow analysis of the associated private company issuers. The valuations of the securities are negatively impacted by projected net losses of the associated private companies and positively impacted by projected net gains.

The fair values of our Level 2 securities available for sale are determined by a third-party pricing service. The valuations provided by the third-party pricing service are based on observable market inputs, which include benchmark yields, reported trades, issuer spreads, benchmark securities, bids, offers, and reference data obtained from market research publications. Inputs used by the third-party pricing service in valuing CMOs and other mortgage-backed securities also include new issue data, monthly payment information, whole loan collateral performance, and To Be Announced prices. In valuations of securities issued by state and political subdivisions, inputs used by the third-party pricing service also include material event notices.

On a monthly basis, we validate the pricing methodologies utilized by our third-party pricing service to ensure the fair value determination is consistent with the applicable accounting guidance and that our assets are properly classified in the fair value hierarchy. To perform this validation, we:

review documentation received from our third-party pricing service regarding the inputs used in their valuations and determine a level assessment for each category of securities;

substantiate actual inputs used for a sample of securities by comparing the actual inputs used by our third-party pricing service to comparable inputs for similar securities; and

substantiate the fair values determined for a sample of securities by comparing the fair values provided by our third-party pricing service to prices from other independent sources for the same and similar securities. We analyze variances and conduct additional research with our third-party pricing service and take appropriate steps based on our findings.

***Private equity and mezzanine investments.*** Private equity and mezzanine investments consist of investments in debt and equity securities through our Real Estate Capital line of business. They include direct investments made in specific properties, as well as indirect investments made in funds that pool assets of many investors to invest in properties. There is no active market for these investments, so we employ other valuation methods. The portion of our Real Estate Capital line of business involved with private equity and mezzanine investments is accounted for as an investment company in accordance with the applicable accounting guidance, whereby all investments are recorded at fair value.

Direct private equity and mezzanine investments are classified as Level 3 assets since our judgment significantly influences the determination of fair value. Our Fund Management, Asset Management, and Accounting groups are responsible for reviewing the valuation models and determining the fair value of these investments on a quarterly basis. Direct investments in properties are initially valued based upon the transaction price. This amount is then adjusted to fair value based on current market conditions using the discounted cash flow method based on the expected investment exit date. The fair values of the assets are reviewed and adjusted quarterly. There were no significant direct equity and mezzanine investments at March 31, 2016, and March 31, 2015.

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The fair value of our indirect investments is based on the most recent value of the capital accounts as reported by the general partners of the funds in which we invest. The calculation to determine the investment's fair value is based on our percentage ownership in the fund multiplied by the net asset value of the fund, as provided by the fund manager. Under the requirements of the Volcker Rule, we will be required to dispose of some or all of our indirect investments. As of March 31, 2016, management has not committed to a plan to sell these investments. Therefore, these investments continue to be valued using the net asset value per share methodology. For more information about the Volcker Rule, see the discussion under the heading "Other Regulatory Developments under the Dodd-Frank Act - Volcker Rule" in the section entitled "Supervision and Regulation" beginning on page 17 of our 2015 Form 10-K.

Investments in real estate private equity funds are included within private equity and mezzanine investments. The main purpose of these funds is to acquire a portfolio of real estate investments that provides attractive risk-adjusted returns and current income for investors. Certain of these investments do not have readily determinable fair values and represent our ownership interest in an entity that follows measurement principles under investment company accounting.

The following table presents the fair value of our indirect investments and related unfunded commitments at March 31, 2016. We did not provide any financial support to investees related to our direct and indirect investments for the three months ended March 31, 2016, and March 31, 2015.

<b>March 31, 2016</b> <i>in millions</i>	<b>Fair Value</b>	<b>Unfunded Commitments</b>
<b>INVESTMENT TYPE</b>		
Indirect investments		
Passive funds <sup>(a)</sup>	\$ 8	\$ 1
Total	\$ 8	\$ 1

(a) We invest in passive funds, which are multi-investor private equity funds. These investments can never be redeemed. Instead, distributions are received through the liquidation of the underlying investments in the funds. Some funds have no restrictions on sale, while others require investors to remain in the fund until maturity. The funds will be liquidated over a period of one to three years. The purpose of KREEC's funding is to allow funds to make additional investments and keep a certain market value threshold in the funds. KREEC is obligated to provide financial support, as all investors are required, to the funds based on its ownership percentage, as noted in the Limited Partnership Agreements.

**Principal investments.** Principal investments consist of investments in equity and debt instruments made by our principal investing entities. They include direct investments (investments made in a particular company) and indirect investments (investments made through funds that include other investors). Our principal investing entities are accounted for as investment companies in accordance with the applicable accounting guidance, whereby each investment is adjusted to fair value with any net realized or unrealized gain/loss recorded in the current period's earnings. This process is a coordinated and documented effort by the Principal Investing Entities Deal Team (individuals from one of the independent investment managers who oversee these instruments), accounting staff, and the Investment Committee (individual employees and a former employee of Key and one of the independent investment managers). This process involves an in-depth review of the condition of each investment depending on the type of investment.

Our direct investments include investments in debt and equity instruments of both private and public companies. When quoted prices are available in an active market for the identical direct investment, we use the quoted prices in the valuation process, and the related investments are classified as Level 1 assets. As of December 31, 2015, the valuation of our Level 2 investment included a quoted price, which was adjusted by liquidity assumptions due to a contractual term of the investment. The contractual term expired and this investment was transferred from Level 2 to Level 1 as of March 31, 2016. In most cases, quoted market prices are not available for our direct investments, and we must perform valuations using other methods. These direct investment valuations are an in-depth analysis of the condition of each investment and are based on the unique facts and circumstances related to each individual investment. There is a certain amount of subjectivity surrounding the valuation of these investments due to the combination of quantitative and qualitative factors that are used in the valuation models. Therefore, these direct investments are classified as Level 3 assets. The specific inputs used in the valuations of each type of direct investment are described below.

Interest-bearing securities (i.e., loans) are valued on a quarterly basis. Valuation adjustments are determined by the Principal Investing Entities Deal Team and are subject to approval by the Investment Committee. Valuations of debt instruments are based on the Principal Investing Entities Deal Team's knowledge of the current financial status of the subject company, which is regularly monitored throughout the term of the investment. Significant unobservable inputs used in the valuations of these investments include the company's payment history, adequacy of cash flows from operations, and current operating results, including market multiples and historical and forecast EBITDA. Inputs can also include the seniority of the debt, the nature of any pledged collateral, the extent to which the security interest is perfected, and the net liquidation value of collateral.

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Valuations of equity instruments of private companies, which are prepared on a quarterly basis, are based on current market conditions and the current financial status of each company. A valuation analysis is performed to value each investment. The valuation analysis is reviewed by the Principal Investing Entities Deal Team Member, and reviewed and approved by the Chief Administrative Officer of one of the independent investment managers. Significant unobservable inputs used in these valuations include adequacy of the company's cash flows from operations, any significant change in the company's performance since the prior valuation, and any significant equity issuances by the company. Equity instruments of public companies are valued using quoted prices in an active market for the identical security. If the instrument is restricted, the fair value is determined considering the number of shares traded daily, the number of the company's total restricted shares, and price volatility.

Our indirect investments include primary and secondary investments in private equity funds engaged mainly in venture- and growth-oriented investing. These investments do not have readily determinable fair values. Indirect investments are valued using a methodology that is consistent with accounting guidance that allows us to estimate fair value based upon net asset value per share (or its equivalent, such as member units or an ownership interest in partners capital to which a proportionate share of net assets is attributed). Under the requirements of the Volcker Rule, we will be required to dispose of some or all of our indirect investments. At March 31, 2016, one of our indirect investments was identified for sale, and management has committed to a plan to sell this identified investment. It is probable that we will sell this investment for an amount different from its net asset value. The investment is valued at its probable sale price as of March 31, 2016. The remaining investments continue to be valued using the net asset value per share methodology.

For indirect investments, management may make adjustments it deems appropriate to the net asset value if it is determined that the net asset value does not properly reflect fair value. In determining the need for an adjustment to net asset value, management performs an analysis of the private equity funds based on the independent fund manager's valuations as well as management's own judgment. Management also considers whether the independent fund manager adequately marks down an impaired investment, maintains financial statements in accordance with GAAP, or follows a practice of holding all investments at cost.

The following table presents the fair value of our direct and indirect principal investments and related unfunded commitments at March 31, 2016, as well as financial support provided for the three months ended March 31, 2016, and March 31, 2015.

<i>in millions</i>	March 31, 2016		Financial support provided Three months ended March 31,			
	Fair Value	Unfunded Commitments	2016	2016	2015	2015
INVESTMENT TYPE			Funded Commitments	Funded Other	Funded Commitments	Funded Other
Direct investments <sup>(a)</sup>	\$ 61			\$ 13		\$ 3
Indirect investments (measured at NAV) <sup>(b)</sup>	211	\$ 47	\$ 1		\$ 2	
Other indirect investment <sup>(b)</sup>	18	3				
<b>Total</b>	<b>\$ 290</b>	<b>\$ 50</b>	<b>\$ 1</b>	<b>\$ 13</b>	<b>\$ 2</b>	<b>\$ 3</b>

- (a) Our direct investments consist of equity and debt investments directly in independent business enterprises. Operations of the business enterprises are handled by management of the portfolio company. The purpose of funding these enterprises is to provide financial support for business development and acquisition strategies. We infuse equity capital based on an initial contractual cash contribution and later from additional requests on behalf of the companies' management.
- (b) Our indirect investments consist of buyout funds, venture capital funds, and fund of funds. These investments are generally not redeemable. Instead, distributions are received through the liquidation of the underlying investments of the fund. An investment in any one of these funds typically can be sold only with the approval of the fund's general partners. We estimate that the underlying investments of the funds will be liquidated over a period of one to eight years. The purpose of funding our capital commitments to these investments is to allow the funds to make additional follow-on investments and pay fund expenses until the fund dissolves. We, and all other investors in the fund, are obligated to fund the full amount of our respective capital commitments to the fund based on our and their respective ownership percentages, as noted in the applicable Limited Partnership Agreement.

**Other.** We had one indirect equity investment in the form of limited partnership units representing less than a five percent ownership interest in the entity's equity. The fair value of this investment was based upon the NAV accounting methodology. Under the requirements of the Volcker Rule, we were required to dispose of this investment. Prior to December 31, 2015, this investment was redeemed.



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**Derivatives.** Exchange-traded derivatives are valued using quoted prices and, therefore, are classified as Level 1 instruments. However, only a few types of derivatives are exchange-traded. The majority of our derivative positions are valued using internally developed models based on market convention that use observable market inputs, such as interest rate curves, yield curves, LIBOR and Overnight Index Swap (OIS) discount rates and curves, index pricing curves, foreign currency curves, and volatility surfaces (a three-dimensional graph of implied volatility against strike price and maturity). These derivative contracts, which are classified as Level 2 instruments, include interest rate swaps, certain options, cross currency swaps, and credit default swaps.

In addition, we have several customized derivative instruments and risk participations that are classified as Level 3 instruments. These derivative positions are valued using internally developed models, with inputs consisting of available market data, such as bond spreads and asset values, as well as unobservable internally derived assumptions, such as loss probabilities and internal risk ratings of customers. These derivatives are priced monthly by our MRM group using a credit valuation adjustment methodology. Swap details with the customer and our related participation percentage, if applicable, are obtained from our derivatives accounting system, which is the system of record. Applicable customer rating information is obtained from the particular loan system and represents an unobservable input to this valuation process. Using these various inputs, a valuation of these Level 3 derivatives is performed using a model that was acquired from a third party. In summary, the fair value represents an estimate of the amount that the risk participation counterparty would need to pay/receive as of the measurement date based on the probability of customer default on the swap transaction and the fair value of the underlying customer swap. Therefore, a higher loss probability and a lower credit rating would negatively affect the fair value of the risk participations and a lower loss probability and higher credit rating would positively affect the fair value of the risk participations.

Market convention implies a credit rating of AA equivalent in the pricing of derivative contracts, which assumes all counterparties have the same creditworthiness. To reflect the actual exposure on our derivative contracts related to both counterparty and our own creditworthiness, we record a fair value adjustment in the form of a credit valuation adjustment. The credit component is determined by individual counterparty based on the probability of default and considers master netting and collateral agreements. The credit valuation adjustment is classified as Level 3. Our MRM group is responsible for the valuation policies and procedures related to this credit valuation adjustment. A weekly reconciliation process is performed to ensure that all applicable derivative positions are covered in the calculation, which includes transmitting customer exposures and reserve reports to trading management, derivative traders and marketers, derivatives middle office, and corporate accounting personnel. On a quarterly basis, MRM prepares the credit valuation adjustment calculation, which includes a detailed reserve comparison with the previous quarter, an analysis for change in reserve, and a reserve forecast to ensure that the credit valuation adjustment recorded at period end is sufficient.

**Other assets and liabilities.** The value of our short positions is driven by the valuation of the underlying securities. If quoted prices for identical securities are not available, fair value is determined by using pricing models or quoted prices of similar securities, resulting in a Level 2 classification. For the interest rate-driven products, such as government bonds, U.S. Treasury bonds and other products backed by the U.S. government, inputs include spreads, credit ratings, and interest rates. For the credit-driven products, such as corporate bonds and mortgage-backed securities, inputs include actual trade data for comparable assets and bids and offers.

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

Certain assets and liabilities are measured at fair value on a recurring basis in accordance with GAAP. The following tables present these assets and liabilities at March 31, 2016, December 31, 2015, and March 31, 2015.



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<i>in millions</i>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>ASSETS MEASURED ON A RECURRING BASIS</b>				
Trading account assets:				
U.S. Treasury, agencies and corporations		\$ 636		\$ 636
States and political subdivisions		26		26
Collateralized mortgage obligations				
Other mortgage-backed securities		64		64
Other securities		37		37
Total trading account securities		763		763
Commercial loans		2		2