KEYCORP /NEW/
Form 10-Q
October 31, 2013
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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 September 30, 2013**

**Commission File Number 1-11302**

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

| **Ohio** | **34-6542451** |
|---|---|
| **State or other jurisdiction of** | **I.R.S. Employer** |

| **incorporation or organization** | **Identification Number:** |
|---|---|
| **127 Public Square, Cleveland, Ohio** | **44114-1306** |
| **Address of principal executive offices:** | **Zip Code:** |

**(216) 689-3000**

**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 x 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 x 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 x | 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 x

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 | 896,671,849 Shares |
|---|---|
| **Title of class** | **Outstanding at October 29, 2013** |

**KEYCORP**

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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 ) that begins on page 10.**

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**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**Consolidated Balance Sheets**

| *in millions, except per share data* | September 30, 2013 (Unaudited) | December 31, 2012 | September 30, 2012 (Unaudited) |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and due from banks | **$ 748** | $ 584 | $ 973 |
| Short-term investments | **3,535** | 3,940 | 2,208 |
| Trading account assets | **806** | 605 | 663 |
| Securities available for sale | **12,606** | 12,094 | 11,962 |
| Held-to-maturity securities (fair value: $4,730, $3,992 and $4,212) | **4,835** | 3,931 | 4,153 |
| Other investments | **1,007** | 1,064 | 1,106 |
| Loans, net of unearned income of $827, $957 and $980 | **53,597** | 52,822 | 51,419 |
| Less: Allowance for loan and lease losses | **868** | 888 | 888 |
| Net loans | **52,729** | 51,934 | 50,531 |
| Loans held for sale | **699** | 599 | 628 |
| Premises and equipment | **890** | 965 | 942 |
| Operating lease assets | **293** | 288 | 290 |
| Goodwill | **979** | 979 | 979 |
| Other intangible assets | **137** | 171 | 182 |
| Corporate-owned life insurance | **3,384** | 3,333 | 3,309 |
| Derivative assets | **475** | 693 | 771 |
| Accrued income and other assets (including $24 of consolidated LIHTC guaranteed funds VIEs, see Note 9) [(a)] | **2,747** | 2,774 | 2,853 |
| Discontinued assets (including $2,158 of consolidated education loan securitization trust VIEs (see Note 9) and $148 of loans in portfolio at fair value) [(a)] | **4,838** | 5,282 | 5,400 |
| Total assets | **$ 90,708** | $ 89,236 | $ 86,950 |
| **LIABILITIES** | | | |
| Deposits in domestic offices: | | | |
| NOW and money market deposit accounts | **$ 33,132** | $ 32,380 | $ 30,573 |
| Savings deposits | **2,489** | 2,433 | 2,393 |
| Certificates of deposit ($100,000 or more) | **2,698** | 2,879 | 3,226 |
| Other time deposits | **3,833** | 4,575 | 4,941 |
| Total interest-bearing | **42,152** | 42,267 | 41,133 |
| Noninterest-bearing | **25,778** | 23,319 | 22,486 |
| Deposits in foreign office interest-bearing | **605** | 407 | 569 |
| Total deposits | **68,535** | 65,993 | 64,188 |
| Federal funds purchased and securities sold under repurchase agreements | **1,455** | 1,609 | 1,746 |
| Bank notes and other short-term borrowings | **466** | 287 | 388 |
| Derivative liabilities | **450** | 584 | 657 |
| Accrued expense and other liabilities | **1,375** | 1,387 | 1,205 |
| Long-term debt | **6,154** | 6,847 | 6,119 |
| Discontinued liabilities (including $2,037 of consolidated education loan securitization trust VIEs at fair value, see Note 9) [(a)] | **2,037** | 2,220 | 2,368 |

| | | | |
|---|---|---|---|
| Total liabilities | **80,472** | 78,927 | 76,671 |
| **EQUITY** | | | |
| 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 2,904,839, 2,904,839 and 2,904,839 shares | **291** | 291 | 291 |
| Common shares, $1 par value; authorized 1,400,000,000 shares; issued 1,016,969,905, 1,016,969,905 and 1,016,969,905 shares | **1,017** | 1,017 | 1,017 |
| Capital surplus | **4,029** | 4,126 | 4,118 |
| Retained earnings | **7,431** | 6,913 | 6,762 |
| Treasury stock, at cost (119,148,654, 91,201,285 and 80,775,030) | **(2,193)** | (1,952) | (1,868) |
| Accumulated other comprehensive income (loss) | **(369)** | (124) | (69) |
| Key shareholders equity | **10,206** | 10,271 | 10,251 |
| Noncontrolling interests | **30** | 38 | 28 |
| Total equity | **10,236** | 10,309 | 10,279 |
| Total liabilities and equity | **$ 90,708** | $ 89,236 | $ 86,950 |

(a) The assets of the VIEs can only be used by the particular VIE and there is no recourse to Key with respect to the liabilities of the consolidated LIHTC or education loan securitization trust VIEs.

See Notes to Consolidated Financial Statements (Unaudited).

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**Consolidated Statements of Income (Unaudited)**

| *dollars in millions, except per share amounts* | Three months ended September 30, 2013 | 2012 | Nine months ended September 30, 2013 | 2012 |
|---|---|---|---|---|
| **INTEREST INCOME** | | | | |
| Loans | **$ 532** | $ 538 | **$ 1,619** | $ 1,592 |
| Loans held for sale | **5** | 5 | **14** | 15 |
| Securities available for sale | **76** | 93 | **236** | 314 |
| Held-to-maturity securities | **22** | 21 | **60** | 50 |
| Trading account assets | **5** | 4 | **15** | 15 |
| Short-term investments | **1** | 1 | **4** | 4 |
| Other investments | **6** | 9 | **23** | 27 |
| Total interest income | **647** | 671 | **1,971** | 2,017 |
| **INTEREST EXPENSE** | | | | |
| Deposits | **37** | 60 | **124** | 208 |
| Federal funds purchased and securities sold under repurchase agreements | **1** | 1 | **2** | 3 |
| Bank notes and other short-term borrowings | **2** | 1 | **5** | 5 |
| Long-term debt | **29** | 37 | **98** | 138 |
| Total interest expense | **69** | 99 | **229** | 354 |
| **NET INTEREST INCOME** | **578** | 572 | **1,742** | 1,663 |
| Provision (credit) for loan and lease losses | **28** | 109 | **111** | 172 |
| Net interest income (expense) after provision for loan and lease losses | **550** | 463 | **1,631** | 1,491 |
| **NONINTEREST INCOME** | | | | |
| Trust and investment services income | **100** | 94 | **295** | 280 |
| Investment banking and debt placement fees | **86** | 83 | **249** | 217 |
| Service charges on deposit accounts | **73** | 74 | **213** | 212 |
| Operating lease income and other leasing gains | **43** | 66 | **85** | 176 |
| Corporate services income | **44** | 39 | **132** | 127 |
| Cards and payments income | **43** | 37 | **122** | 97 |
| Corporate-owned life insurance income | **26** | 26 | **87** | 86 |
| Consumer mortgage income | **3** | 11 | **16** | 29 |
| Net gains (losses) from principal investing | **17** | 11 | **32** | 70 |
| Other income [(a)] | **24** | 77 | **82** | 123 |
| Total noninterest income | **459** | 518 | **1,313** | 1,417 |
| **NONINTEREST EXPENSE** | | | | |
| Personnel | **414** | 399 | **1,211** | 1,148 |
| Net occupancy | **66** | 65 | **202** | 191 |
| Computer processing | **38** | 42 | **116** | 126 |
| Business services and professional fees | **37** | 48 | **109** | 136 |
| Equipment | **25** | 27 | **78** | 80 |
| Operating lease expense | **14** | 13 | **37** | 45 |
| Marketing | **16** | 18 | **33** | 48 |
| FDIC assessment | **7** | 7 | **23** | 23 |
| Intangible asset amortization on credit cards | **8** | 6 | **23** | 6 |
| Other intangible asset amortization | **4** | 3 | **11** | 5 |
| Provision (credit) for losses on lending-related commitments | **3** | (8) | **11** | (2) |
| OREO expense, net | **1** | 1 | **5** | 14 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Other expense | | **83** | | 91 | | **249** | | 264 |
| Total noninterest expense | | **716** | | 712 | | **2,108** | | 2,084 |
| **INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES** | | **293** | | 269 | | **836** | | 824 |
| Income taxes | | **59** | | 51 | | **201** | | 178 |
| **INCOME (LOSS) FROM CONTINUING OPERATIONS** | | **234** | | 218 | | **635** | | 646 |
| Income (loss) from discontinued operations, net of taxes of $21, $1, $29, and $9 (see Note 11) | | **37** | | 3 | | **45** | | 16 |
| **NET INCOME (LOSS)** | | **271** | | 221 | | **680** | | 662 |
| Less: Net income (loss) attributable to noncontrolling interests | | **(1)** | | 2 | | | | 7 |
| **NET INCOME (LOSS) ATTRIBUTABLE TO KEY** | **$** | **272** | $ | 219 | **$** | **680** | $ | 655 |
| Income (loss) from continuing operations attributable to Key common shareholders | **$** | **229** | $ | 211 | **$** | **618** | $ | 623 |
| Net income (loss) attributable to Key common shareholders | | **266** | | 214 | | **663** | | 639 |
| Per common share: | | | | | | | | |
| Income (loss) from continuing operations attributable to Key common shareholders | **$** | **.25** | $ | .23 | **$** | **.68** | $ | .66 |
| Income (loss) from discontinued operations, net of taxes | | **.04** | | | | **.05** | | .02 |
| Net income (loss) attributable to Key common shareholders [b] | | **.29** | | .23 | | **.73** | | .68 |
| Per common share assuming dilution: | | | | | | | | |
| Income (loss) from continuing operations attributable to Key common shareholders | **$** | **.25** | $ | .22 | **$** | **.67** | $ | .66 |
| Income (loss) from discontinued operations, net of taxes | | **.04** | | | | **.05** | | .02 |
| Net income (loss) attributable to Key common shareholders [b] | | **.29** | | .23 | | **.72** | | .67 |
| Cash dividends declared per common share | **$** | **.055** | $ | .05 | **$** | **.16** | $ | .13 |
| Weighted-average common shares outstanding (000) | | **901,904** | | 936,223 | | **911,918** | | 943,378 |
| Weighted-average common shares and potential common shares outstanding (000) [c] | | **928,854** | | 940,764 | | **917,579** | | 947,582 |

(a) For the three months ended September 30, 2013 and 2012, we did not have any impairment losses related to securities.
(b) EPS may not foot due to rounding.
(c) Assumes conversion of stock options and/or Series A Preferred Stock, as applicable.
See Notes to Consolidated Financial Statements (Unaudited).

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

| *in millions* | Three months ended September 30, 2013 | Three months ended September 30, 2012 | Nine months ended September 30, 2013 | Nine months ended September 30, 2012 |
|---|---|---|---|---|
| Net income (loss) | **$ 271** | $ 221 | **$ 680** | $ 662 |
| Other comprehensive income (loss), net of tax: | | | | |
| Net unrealized gains (losses) on securities available for sale, net of income taxes of ($48), ($17), ($135) and ($48) | **(81)** | (28) | **(228)** | (81) |
| Net unrealized gains (losses) on derivative financial instruments, net of income taxes of $6, $12, ($17) and $17 | **10** | 20 | **(29)** | 28 |
| Foreign currency translation adjustments, net of income taxes | **2** | 9 | **(12)** | 5 |
| Net pension and postretirement benefit costs, net of income taxes | **18** | 2 | **24** | 7 |
| Total other comprehensive income (loss), net of tax | **(51)** | 3 | **(245)** | (41) |
| Comprehensive income (loss) | **220** | 224 | **435** | 621 |
| Less: Comprehensive income attributable to noncontrolling interests | **(1)** | 2 | | 7 |
| Comprehensive income (loss) attributable to Key | **$ 221** | $ 222 | **$ 435** | $ 614 |

See Notes to Consolidated Financial Statements (Unaudited).

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**Consolidated Statements of Changes in Equity (Unaudited)**

| | Key Shareholders Equity | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| *dollars in millions, except per share amounts* | Preferred Shares Outstanding (000) | Common Shares Outstanding (000) | Preferred Stock | Common Shares | Capital Surplus | Retained Earnings | Treasury Stock, at Cost | Accumulated Other Comprehensive Income (Loss) | Noncontrolling Interests |
| **BALANCE AT DECEMBER 31, 2011** | 2,905 | 953,008 | $ 291 | $ 1,017 | $ 4,194 | $ 6,246 | $ (1,815) | $ (28) | $ 17 |
| Net income (loss) | | | | | | 655 | | | 7 |
| Other comprehensive income (loss): | | | | | | | | | |
| Net unrealized gains (losses) on securities available for sale, net of income taxes of ($48) | | | | | | | | (81) | |
| Net unrealized gains (losses) on derivative financial instruments, net of income taxes of $17 | | | | | | | | 28 | |
| Foreign currency translation adjustments, net of income taxes | | | | | | | | 5 | |
| Net pension and postretirement benefit costs, net of income taxes | | | | | | | | 7 | |
| Deferred compensation | | | | | 10 | | | | |
| Cash dividends declared on common shares ($.13 per share) | | | | | | (123) | | | |
| Cash dividends declared on Noncumulative Series A Preferred Stock ($5.8125 per share) | | | | | | (16) | | | |
| Common shares repurchased | | (20,107) | | | | | (163) | | |
| Common shares reissued (returned) for stock options and other employee benefit plans | | 3,294 | | | (86) | | 110 | | |
| Net contribution from (distribution to) noncontrolling interests | | | | | | | | | 4 |
| **BALANCE AT SEPTEMBER 30, 2012** | 2,905 | 936,195 | $ 291 | $ 1,017 | $ 4,118 | $ 6,762 | $ (1,868) | $ (69) | $ 28 |
| **BALANCE AT DECEMBER 31, 2012** | 2,905 | 925,769 | $ 291 | $ 1,017 | $ 4,126 | $ 6,913 | $ (1,952) | $ (124) | $ 38 |
| Net income (loss) | | | | | | **680** | | | |
| Other comprehensive income (loss): | | | | | | | | | |
| Net unrealized gains (losses) on securities available for sale, net of income taxes of ($135) | | | | | | | | **(228)** | |
| Net unrealized gains (losses) on derivative financial instruments, net of income taxes of ($17) | | | | | | | | **(29)** | |
| Foreign currency translation adjustments, net of income taxes | | | | | | | | **(12)** | |
| Net pension and postretirement benefit costs, net of income taxes | | | | | | | | **24** | |
| Deferred compensation | | | | | **3** | | | | |
| Cash dividends declared on common shares ($.16 per share) | | | | | | **(145)** | | | |
| Cash dividends declared on Noncumulative Series A Preferred Stock ($5.8125 per share) | | | | | | **(17)** | | | |
| Common shares repurchased | | **(33,940)** | | | | | **(375)** | | |
| Common shares reissued (returned) for stock options and other employee benefit plans | | **5,992** | | | **(100)** | | **134** | | |
| Net contribution from (distribution to) noncontrolling interests | | | | | | | | | **(8)** |
| **BALANCE AT SEPTEMBER 30, 2013** | **2,905** | **897,821** | **$ 291** | **$ 1,017** | **$ 4,029** | **$ 7,431** | **$ (2,193)** | **$ (369)** | **$ 30** |

See Notes to Consolidated Financial Statements (Unaudited).

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

| *in millions* | Nine months ended September 30, 2013 | 2012 |
|---|---|---|
| **OPERATING ACTIVITIES** | | |
| Net income (loss) | $ **680** | $ 662 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | |
| Provision (credit) for loan and lease losses | **111** | 172 |
| Provision (credit) for losses on lending-related commitments | **11** | (2) |
| Provision (credit) for losses on LIHTC guaranteed funds | **4** | |
| Depreciation, amortization and accretion expense, net | **147** | 162 |
| Stock-based compensation expense | **27** | 38 |
| FDIC (payments) net of FDIC expense | **296** | 19 |
| Deferred income taxes (benefit) | **(4)** | 36 |
| Proceeds from sales of loans held for sale | **3,821** | 3,737 |
| Originations of loans held for sale, net of repayments | **(3,779)** | (3,507) |
| Net losses (gains) on sales of loans held for sale | **(91)** | (93) |
| Net losses (gains) from principal investing | **(32)** | (70) |
| Net losses (gains) and writedown on OREO | **5** | 12 |
| Net losses (gains) on leased equipment | **(36)** | (109) |
| Net losses (gains) on sales of fixed assets | **9** | |
| Net decrease (increase) in trading account assets | **(201)** | (40) |
| Other operating activities, net | **52** | (369) |
| NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES | **1,020** | 648 |
| **INVESTING ACTIVITIES** | | |
| Cash received (used) in acquisitions, net of cash acquired | **817** | 866 |
| Proceeds from sale of Victory | **72** | |
| Gain on sale of Victory | **(92)** | |
| Net decrease (increase) in short-term investments | **405** | 1,311 |
| Purchases of securities available for sale | **(4,628)** | (232) |
| Proceeds from sales of securities available for sale | **29** | 1 |
| Proceeds from prepayments and maturities of securities available for sale | **3,725** | 4,159 |
| Proceeds from prepayments and maturities of held-to-maturity securities | **667** | 437 |
| Purchases of held-to-maturity securities | **(1,572)** | (2,481) |
| Purchases of other investments | **(30)** | (48) |
| Proceeds from sales of other investments | **39** | 17 |
| Proceeds from prepayments and maturities of other investments | **82** | 134 |
| Net decrease (increase) in loans, excluding acquisitions, sales and transfers | **(1,077)** | (1,342) |
| Proceeds from sales of portfolio loans | **150** | 207 |
| Purchases of premises and equipment | **(60)** | (101) |
| Proceeds from sales of premises and equipment | **8** | 1 |
| Proceeds from sales of other real estate owned | **19** | 55 |
| NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES | **(1,446)** | 2,984 |
| **FINANCING ACTIVITIES** | | |
| Net increase (decrease) in deposits, excluding acquisitions | **1,605** | 184 |
| Net increase (decrease) in short-term borrowings | **26** | 86 |
| Net proceeds from issuance of long-term debt | **1,013** | 59 |
| Payments on long-term debt | **(1,540)** | (3,381) |
| Repurchase of Common Shares | **(375)** | (163) |
| Net proceeds from reissuance of Common Shares | **22** | 2 |
| Tax benefits in excess of reorganized compensation costs for share-based payment | **1** | |
| Cash dividends paid | **(162)** | (139) |

| | | | | |
|---|---|---|---|---|
| NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES | | **590** | | (3,352) |
| | | | | |
| **NET INCREASE (DECREASE) IN CASH AND DUE FROM BANKS** | | **164** | | 280 |
| **CASH AND DUE FROM BANKS AT BEGINNING OF PERIOD** | | **584** | | 693 |
| | | | | |
| **CASH AND DUE FROM BANKS AT END OF PERIOD** | $ | **748** | $ | 973 |
| | | | | |
| Additional disclosures relative to cash flows: | | | | |
| Interest paid | $ | **271** | $ | 302 |
| Income taxes paid (refunded) | | **114** | | 39 |
| Noncash items: | | | | |
| Assets acquired | $ | **41** | $ | 1,194 |
| Liabilities assumed | | | | 2,059 |
| Loans transferred to portfolio from held for sale | | **2** | | 41 |
| Loans transferred to held for sale from portfolio | | **53** | | 80 |
| Loans transferred to other real estate owned | | **16** | | 32 |

See Notes to Consolidated Financial Statements (Unaudited).

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## Notes to Consolidated Financial Statements (Unaudited)

### 1. Basis of Presentation

As used in these Notes, references to Key, we, our, us and similar terms refer to the consolidated entity 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 2012 Form 10-K refer to our Form 10-K for the year ended December 31, 2012, that has been filed with the U.S. Securities and Exchange Commission and is available on its website (www.sec.gov) or on our website (www.key.com/ir).

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ABO: Accumulated benefit obligation.
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.
BHCA: Bank Holding Company Act of 1956, as amended.
BHCs: Bank holding companies.
CCAR: Comprehensive Capital Analysis and Review.
CFPB: Bureau of Consumer Financial Protection.
CFTC: Commodities Futures Trading Commission.
CMBS: Commercial mortgage-backed securities.
CMO: Collateralized mortgage obligation.
Common Shares: Common Shares, $1 par value.
CPP: Capital Purchase Program of the U.S. Treasury.
DIF: Deposit Insurance Fund of the FDIC.
Dodd-Frank Act: Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.
ERISA: Employee Retirement Income Security Act of 1974.
ERM: Enterprise risk management.
EVE: Economic value of equity.
FASB: Financial Accounting Standards Board.
FDIA: Federal Deposit Insurance Act, as amended.
FDIC: Federal Deposit Insurance Corporation.
Federal Reserve: Board of Governors of the Federal Reserve System.
FHFA: Federal Housing Finance Agency.
FHLMC: Federal Home Loan Mortgage Corporation.
FINRA: Financial Industry Regulatory Authority.
FNMA: Federal National Mortgage Association.
FOMC: Federal Open Market Committee of the Federal Reserve Board.
FSOC: Financial Stability Oversight Council.
FVA: Fair value of pension plan assets.
GAAP: U.S. generally accepted accounting principles.
GNMA: Government National Mortgage Association.
HUD: U.S. Department of Housing and Urban Development.
IRS: Internal Revenue Service.
ISDA: International Swaps and Derivatives Association.
KAHC: Key Affordable Housing Corporation.
LIBOR: London Interbank Offered Rate.
LIHTC: Low-income housing tax credit.
LILO: Lease in, lease out transaction.
Moody s: Moody s Investor Services, Inc.
MSRs: Mortgage servicing rights.
N/A: Not applicable.
NASDAQ: The NASDAQ Stock Market LLC.
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).
OFR: Office of Financial Research of the U.S. Department of Treasury.
OREO: Other real estate owned.
OTTI: Other-than-temporary impairment.
QSPE: Qualifying special purpose entity.
PBO: Projected benefit obligation.
PCCR: Purchased credit card relationship.
PCI: Purchased credit impaired.
S&P: Standard and Poor s Ratings Services, a Division of The McGraw-Hill Companies, Inc.
SCAP: Supervisory Capital Assessment Program administered by the Federal Reserve.
SEC: U.S. Securities & Exchange Commission.
Series A Preferred Stock: KeyCorp s 7.750% Noncumulative Perpetual Convertible Preferred Stock, Series A.
SIFIs: Systemically important financial companies, including BHCs with total consolidated assets of at least $50 billion and nonbank financial companies designated by FSOC for supervision by the Federal Reserve.
SILO: Sale in, lease out transaction.
SPE: Special purpose entity.
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.
Victory: Victory Capital Management and/or Victory Capital Advisors.
VIE: Variable interest entity.
XBRL: eXtensible Business Reporting Language.

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.

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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 (primarily principal investments) 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 2012 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 2013**

***Benchmark interest rate.*** In July 2013, the FASB issued new accounting guidance allowing entities to designate the Federal Funds Effective Swap Rate (which is the Overnight Index Swap rate, or OIS rate, in the U.S.) as a benchmark interest rate, in addition to U.S. Treasury and LIBOR rates, for hedge accounting purposes. This new accounting guidance was effective prospectively for qualifying new or redesignated hedging relationships entered into on or after July 17, 2013 (effective July 17, 2013, for us). Note 7 ( Derivatives and Hedging Activities ) provides information regarding our use of derivatives and hedge accounting.

***Reporting of amounts reclassified out of AOCI.*** In February 2013, the FASB issued new accounting guidance that requires reclassifications of amounts out of AOCI to be reported in a new format. It does not require the reporting of any information that is not currently required to be disclosed under existing GAAP. This accounting guidance was effective prospectively for reporting periods beginning after December 15, 2012 (effective January 1, 2013, for us). The disclosures required by this accounting guidance are provided in Note 16 ( Accumulated Other Comprehensive Income ).

***Testing indefinite-lived intangible assets for impairment.*** In July 2012, the FASB issued new accounting guidance that simplifies how an entity tests indefinite-lived intangible assets other than goodwill for impairment. It permits an entity to first assess qualitative factors to determine whether further testing for impairment of indefinite-lived intangible assets other than goodwill is required. This accounting guidance was effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012 (January 1, 2013, for us). The adoption of this accounting guidance did not have a material effect on our financial condition or results of operations.

***Offsetting disclosures.*** In December 2011, the FASB issued new accounting guidance that requires an entity to disclose information about offsetting and related arrangements to enable financial statement users to understand the effect of those arrangements on the entity s financial position. In January 2013, the FASB issued new accounting guidance that clarified the scope of the guidance to include derivatives, repurchase and reverse repurchase agreements, and securities lending and borrowing transactions. This accounting guidance was effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods (effective January 1, 2013, for us). Information about our offsetting and related arrangements is provided in Note 12 ( Securities Financing Activities ).

**Accounting Guidance Pending Adoption at September 30, 2013**

***Presentation of unrecognized tax benefits.*** In July 2013, the FASB issued new accounting guidance that requires unrecognized tax benefits to be presented as a decrease in a net operating loss, similar tax loss or tax credit carryforward if

certain criteria are met. This accounting guidance will be applied prospectively to unrecognized tax benefits that exist at the effective date. It will be effective for fiscal years, and interim periods within those years, beginning after December 15, 2013 (effective January 1, 2014, for us). Early adoption and/or retrospective application are permitted. The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

***Investment companies.*** In June 2013, the FASB issued new accounting guidance that modifies the criteria used in defining an investment company. It also sets forth certain measurement and disclosure requirements for an investment company. This accounting guidance will be effective for interim and annual reporting periods in fiscal years that begin after December 15, 2013 (effective January 1, 2014, for us). Early application is prohibited. We are currently evaluating the impact this accounting guidance may have on our financial condition or results of operations.

***Liquidation basis of accounting.*** In April 2013, the FASB issued new accounting guidance that specifies when and how an entity should prepare its financial statements using the liquidation basis of accounting when liquidation is imminent as defined in the guidance and describes the related disclosures that should be made. This new accounting guidance will be effective for entities that determine liquidation is imminent during annual reporting periods beginning after December 15, 2013, and interim reporting periods therein (effective January 1, 2014, for us). Entities should apply the requirements prospectively from the day that liquidation becomes imminent. Early adoption is permitted.

***Reporting of cumulative translation adjustments upon the derecognition of certain investments.*** In March 2013, the FASB issued new accounting guidance that addresses the accounting for the cumulative translation adjustment when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. This accounting guidance will be effective prospectively for reporting periods beginning after December 15, 2013 (effective January 1, 2014, for us). The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

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### 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. For the three months ended September 30, 2013, weighted-average common shares and potential common shares outstanding included 20.6 million shares associated with the conversion of our Series A Preferred Stock and 6.4 million shares associated with common share options and other stock awards.

Our basic and diluted earnings per Common Share are calculated as follows:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| *dollars in millions, except per share amounts* | **2013** | **2012** | **2013** | **2012** |
| **EARNINGS** | | | | |
| Income (loss) from continuing operations | **$ 234** | $ 218 | **$ 635** | $ 646 |
| Less: Net income (loss) attributable to noncontrolling interests | **(1)** | 2 | | 7 |
| Income (loss) from continuing operations attributable to Key | **235** | 216 | **635** | 639 |
| Less: Dividends on Series A Preferred Stock | **6** | 5 | **17** | 16 |
| Income (loss) from continuing operations attributable to Key common shareholders | **229** | 211 | **618** | 623 |
| Income (loss) from discontinued operations, net of taxes [a] | **37** | 3 | **45** | 16 |
| Net income (loss) attributable to Key common shareholders | **$ 266** | $ 214 | **$ 663** | $ 639 |
| **WEIGHTED-AVERAGE COMMON SHARES** | | | | |
| Weighted-average common shares outstanding (000) | **901,904** | 936,223 | **911,918** | 943,378 |
| Effect of dilutive convertible preferred stock, common share options and other stock awards (000) | **26,950** | 4,541 | **5,661** | 4,204 |
| Weighted-average common shares and potential common shares outstanding (000) | **928,854** | 940,764 | **917,579** | 947,582 |
| **EARNINGS PER COMMON SHARE** | | | | |
| Income (loss) from continuing operations attributable to Key common shareholders | **$ .25** | $ .23 | **$ .68** | $ .66 |
| Income (loss) from discontinued operations, net of taxes [a] | **.04** | | **.05** | .02 |
| Net income (loss) attributable to Key common shareholders [b] | **.29** | .23 | **.73** | .68 |
| Income (loss) from continuing operations attributable to Key common shareholders assuming dilution | **$ .25** | $ .22 | **$ .67** | $ .66 |
| Income (loss) from discontinued operations, net of taxes [a] | **.04** | | **.05** | .02 |
| Net income (loss) attributable to Key common shareholders assuming dilution [b] | **.29** | .23 | **.72** | .67 |

(a)

In April 2009, we decided to wind down the operations of Austin, a subsidiary that specialized in managing hedge fund investments for institutional customers. In September 2009, we decided to discontinue the education lending business conducted through Key Education Resources, the education payment and financing unit of KeyBank. In February 2013, we decided to sell Victory to a private equity fund. As a result of these decisions, we have accounted for these businesses as discontinued operations. For further discussion regarding the income (loss) from discontinued operations see Note 11 ( Acquisitions and Discontinued Operations ).

(b) EPS may not foot due to rounding.

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### 3. Loans and Loans Held for Sale

Our loans by category are summarized as follows:

| *in millions* | September 30, 2013 | December 31, 2012 | September 30, 2012 |
|---|---|---|---|
| Commercial, financial and agricultural [(a)] | $ **24,317** | $ 23,242 | $ 21,979 |
| Commercial real estate: | | | |
| Commercial mortgage | **7,544** | 7,720 | 7,529 |
| Construction | **1,058** | 1,003 | 1,067 |
| Total commercial real estate loans | **8,602** | 8,723 | 8,596 |
| Commercial lease financing | **4,550** | 4,915 | 4,960 |
| Total commercial loans | **37,469** | 36,880 | 35,535 |
| Residential prime loans: | | | |
| Real estate residential mortgage | **2,198** | 2,174 | 2,138 |
| Home equity: | | | |
| Key Community Bank | **10,285** | 9,816 | 9,768 |
| Other | **353** | 423 | 409 [(d)] |
| Total home equity loans | **10,638** | 10,239 | 10,177 |
| Total residential prime loans | **12,836** | 12,413 | 12,315 |
| Consumer other Key Community Bank | **1,440** | 1,349 | 1,313 |
| Credit cards | **698** | 729 | 710 |
| Consumer other: | | | |
| Marine | **1,083** | 1,358 | 1,448 |
| Other | **71** | 93 | 98 |
| Total consumer other | **1,154** | 1,451 | 1,546 |
| Total consumer loans | **16,128** | 15,942 | 15,884 |
| Total loans [(b) (c)] | $ **53,597** | $ 52,822 | $ 51,419 |

(a) September 30, 2013, December 31, 2012, and September 30, 2012 loan balances include $96 million, $90 million, and $88 million of commercial credit card balances, respectively.

(b) Excluded at September 30, 2013, December 31, 2012, and September 30, 2012, are loans in the amount of $4.7 billion, $5.2 billion, and $5.3 billion, respectively, related to the discontinued operations of the education lending business.

(c) September 30, 2013 loan balance includes purchased loans of $176 million of which $18 million were PCI loans. December 31, 2012 loan balance includes purchased loans of $217 million of which $23 million were PCI loans. September 30, 2012 loan balance includes purchased loans of $231 million of which $25 million were PCI loans.

(d) This loan category was impacted by $45 million in net loan charge-offs taken during the third quarter of 2012 related to updated regulatory guidance.

Our loans held for sale are summarized as follows:

| *in millions* | September 30, 2013 | December 31, 2012 | September 30, 2012 |
|---|---|---|---|

| | | | |
|---|---|---|---|
| Commercial, financial and agricultural | $ **68** | $ 29 | $ 13 |
| Real estate commercial mortgage | **608** | 477 | 484 |
| Real estate construction | | | 10 |
| Commercial lease financing | | 8 | 4 |
| Real estate residential mortgage | **23** | 85 | 117 |
| Total loans held for sale | $ **699** | $ 599 | $ 628 |

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

| *in millions* | September 30, 2013 | December 31, 2012 | September 30, 2012 |
|---|---|---|---|
| Balance at beginning of the period | **$ 402** | $ 628 | $ 656 |
| New originations | **1,467** | 1,686 | 1,280 |
| Transfers from held to maturity, net | **15** | 38 | 13 |
| Loan sales | **(1,181)** | (1,747) | (1,311) |
| Loan draws (payments), net | **(4)** | (4) | (9) |
| Transfers to OREO / valuation adjustments | | (2) | (1) |
| Balance at end of period | **$ 699** | $ 599 | $ 628 |

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## 4. Asset Quality

We manage our exposure to credit risk by closely monitoring loan performance trends and general economic conditions. An indicator of potential credit losses is the level of nonperforming assets and past due loans.

Our nonperforming assets and past due loans were as follows:

| *in millions* | September 30, 2013 | December 31, 2012 | September 30, 2012 |
|---|---|---|---|
| Total nonperforming loans [(a), (b)] | **$ 541** | $ 674 | $ 653 |
| Nonperforming loans held for sale | **13** | 25 | 19 |
| OREO | **15** | 22 | 29 |
| Other nonperforming assets | **10** | 14 | 17 |
| Total nonperforming assets | **$ 579** | $ 735 | $ 718 |
| Nonperforming assets from discontinued operations education lending [(c)] | **$ 23** | $ 20 | $ 22 |
| Restructured loans included in nonperforming loans [(a)] | **$ 228** | $ 249 | $ 217 |
| Restructured loans with an allocated specific allowance [(d)] | **104** | 114 | 78 |
| Specifically allocated allowance for restructured loans [(e)] | **46** | 33 | 31 |
| Accruing loans past due 90 days or more | **$ 90** | $ 78 | $ 89 |
| Accruing loans past due 30 through 89 days | **288** | 424 | 354 |

(a) December 31, 2012 and September 30, 2012 loan balance includes $72 million and $38 million of current, paying as originally agreed, secured loans respectively, that were discharged through Chapter 7 bankruptcy and not formally re-affirmed, as addressed in updated regulatory guidance issued in the third quarter of 2012. Such loans have been designated as nonperforming and TDRs.
(b) September 30, 2013, December 31, 2012 and September 30, 2012 loan balances exclude $18 million, $23 million and $25 million of PCI loans, respectively.
(c) Includes approximately $11 million, $3 million and $3 million of restructured loans at September 30, 2013, December 31, 2012 and September 30, 2012, respectively. See Note 11 ( Acquisitions and Discontinued Operations ) for further discussion.
(d) Included in individually impaired loans allocated a specific allowance.
(e) 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. At the date of acquisition, the estimated gross contractual amount receivable of PCI loans totaled $41 million. The estimated cash flows not expected to be collected (the nonaccretable amount) was $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 September 30, 2013, the outstanding unpaid principal balance and carrying value of all PCI loans was $25 million and $18 million, respectively. Changes in the accretable yield during 2013 included accretion of $1 million and net reclassifications of $1 million, resulting in an ending balance of $5 million at September 30, 2013.

At September 30, 2013, the approximate carrying amount of our commercial nonperforming loans outstanding represented 61% of their original contractual amount, total nonperforming loans outstanding represented 74% of their original contractual amount owed, and nonperforming assets in total were carried at 72% of their original contractual amount.

At September 30, 2013, our twenty largest nonperforming loans totaled $119 million, representing 22% of total loans on nonperforming status from continuing operations. At September 30, 2012, the twenty largest nonperforming loans totaled $202 million, representing 31% of total loans on nonperforming status.

Nonperforming loans and loans held for sale reduced expected interest income by $18 million for the nine months ended September 30, 2013, and $25 million for the year ended December 31, 2012.

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The following tables set forth a further breakdown of individually impaired loans as of September 30, 2013, December 31, 2012 and September 30, 2012:

| **September 30, 2013** *in millions* | **Recorded Investment** [(a)] | **Unpaid Principal Balance** [(b)] | **Specific Allowance** | **Average Recorded Investment** |
|---|---|---|---|---|
| With no related allowance recorded: | | | | |
| Commercial, financial and agricultural | $ 58 | $ 116 | | $ 74 |
| Commercial real estate: | | | | |
| Commercial mortgage | 43 | 80 | | 66 |
| Construction | 41 | 124 | | 45 |
| Total commercial real estate loans | 84 | 204 | | 111 |
| Total commercial loans with no related allowance recorded | 142 | 320 | | 185 |
| Real estate residential mortgage | 16 | 16 | | 16 |
| Home equity: | | | | |
| Key Community Bank | 69 | 69 | | 69 |
| Other | 2 | 2 | | 2 |
| Total home equity loans | 71 | 71 | | 71 |
| Consumer other: | | | | |
| Marine | 3 | 3 | | 3 |
| Total consumer other | 3 | 3 | | 3 |
| Total consumer loans | 90 | 90 | | 90 |
| Total loans with no related allowance recorded | 232 | 410 | | 275 |
| With an allowance recorded: | | | | |
| Commercial, financial and agricultural | 50 | 51 | $ 17 | 36 |
| Commercial real estate: | | | | |
| Commercial mortgage | 3 | 3 | 1 | 4 |
| Construction | 3 | 13 | | 2 |
| Total commercial real estate loans | 6 | 16 | 1 | 6 |
| Total commercial loans with an allowance recorded | 56 | 67 | 18 | 42 |
| Real estate residential mortgage | 20 | 20 | 6 | 20 |
| Home equity: | | | | |
| Key Community Bank | 33 | 33 | 10 | 32 |
| Other | 11 | 11 | 2 | 10 |
| Total home equity loans | 44 | 44 | 12 | 42 |
| Consumer other Key Community Bank | 3 | 3 | | 3 |
| Credit cards | 6 | 6 | 1 | 5 |
| Consumer other: | | | | |
| Marine | 49 | 49 | 10 | 50 |
| Other | 1 | 1 | | 1 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Total consumer other | | 50 | | 50 | | 10 | | 51 |
| Total consumer loans | | 123 | | 123 | | 29 | | 121 |
| Total loans with an allowance recorded | | 179 | | 190 | | 47 | | 163 |
| Total | $ | 411 | $ | 600 | $ | 47 | $ | 438 |

(a) The Recorded Investment in impaired loans 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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| December 31, 2012<br>*in millions* | Recorded Investment [a] | Unpaid Principal Balance [b] | Specific Allowance | Average Recorded Investment |
|---|---|---|---|---|
| With no related allowance recorded: | | | | |
| Commercial, financial and agricultural | $ 32 | $ 64 | | $ 60 |
| Commercial real estate: | | | | |
| Commercial mortgage | 89 | 142 | | 95 |
| Construction | 48 | 182 | | 39 |
| Total commercial real estate loans | 137 | 324 | | 134 |
| Total commercial loans with no related allowance recorded | 169 | 388 | | 194 |
| Real estate residential mortgage | 21 | 21 | | 10 |
| Home equity: | | | | |
| Key Community Bank | 65 | 65 | | 33 |
| Other | 3 | 3 | | 1 |
| Total home equity loans | 68 | 68 | | 34 |
| Total consumer loans | 89 | 89 | | 44 |
| Total loans with no related allowance recorded | 258 | 477 | | 238 |
| With an allowance recorded: | | | | |
| Commercial, financial and agricultural | 33 | 42 | $ 12 | 48 |
| Commercial real estate: | | | | |
| Commercial mortgage | 7 | 7 | 1 | 51 |
| Construction | | | | 6 |
| Total commercial real estate loans | 7 | 7 | 1 | 57 |
| Total commercial loans with an allowance recorded | 40 | 49 | 13 | 105 |
| Real estate residential mortgage | 17 | 17 | 1 | 8 |
| Home equity: | | | | |
| Key Community Bank | 22 | 22 | 11 | 11 |
| Other | 9 | 9 | 1 | 5 |
| Total home equity loans | 31 | 31 | 12 | 16 |
| Consumer other Key Community Bank | 2 | 2 | 2 | 1 |
| Credit cards | 2 | 2 | | 1 |
| Consumer other: | | | | |
| Marine | 60 | 60 | 7 | 30 |
| Other | 1 | 1 | | 1 |
| Total consumer other | 61 | 61 | 7 | 31 |
| Total consumer loans | 113 | 113 | 22 | 57 |
| Total loans with an allowance recorded | 153 | 162 | 35 | 162 |
| Total | $ 411 | $ 639 | $ 35 | $ 400 |

(a) The Recorded Investment in impaired loans 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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| September 30, 2012<br>*in millions* | Recorded Investment [a] | Unpaid Principal Balance [b] | Specific Allowance | Average Recorded Investment |
|---|---|---|---|---|
| With no related allowance recorded: | | | | |
| Commercial, financial and agricultural | $ 57 | $ 118 | | $ 58 |
| Commercial real estate: | | | | |
| Commercial mortgage | 106 | 182 | | 109 |
| Construction | 42 | 203 | | 47 |
| Total commercial real estate loans | 148 | 385 | | 156 |
| Total commercial loans with no related allowance recorded | 205 | 503 | | 214 |
| Real estate residential mortgage | | | | 1 |
| Home equity: | | | | |
| Key Community Bank | 45 | 45 | | 23 |
| Other | 2 | 2 | | 1 |
| Total home equity loans | 47 | 47 | | 24 |
| Consumer other Key Community Bank | 1 | 1 | | 1 |
| Consumer other: | | | | |
| Marine | 4 | 4 | | 2 |
| Total consumer other | 4 | 4 | | 2 |
| Total consumer loans | 52 | 52 | | 28 |
| Total loans with no related allowance recorded | 257 | 555 | | 242 |
| With an allowance recorded: | | | | |
| Commercial, financial and agricultural | 35 | 45 | $ 12 | 39 |
| Commercial real estate: | | | | |
| Commercial mortgage | 31 | 32 | 7 | 44 |
| Construction | | | | 2 |
| Total commercial real estate loans | 31 | 32 | 7 | 46 |
| Total commercial loans with an allowance recorded | 66 | 77 | 19 | 85 |
| Real estate residential mortgage | 18 | 18 | 1 | 17 |
| Home equity: | | | | |
| Key Community Bank | 20 | 20 | 10 | 16 |
| Other | 8 | 8 | 1 | 7 |
| Total home equity loans | 28 | 28 | 11 | 23 |
| Consumer other Key Community Bank | 2 | 2 | 1 | 2 |
| Consumer other: | | | | |
| Marine | 56 | 56 | 7 | 53 |
| Other | 1 | 1 | | 1 |
| Total consumer other | 57 | 57 | 7 | 54 |
| Total consumer loans | 105 | 105 | 20 | 96 |

| | | | | |
|---|---|---|---|---|
| Total loans with an allowance recorded | 171 | 182 | 39 | 181 |
| Total | $ 428 | $ 737 | $ 39 | $ 423 |

(a) The Recorded Investment in impaired loans 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 nine months ended September 30, 2013, and 2012, interest income recognized on the outstanding balances of accruing impaired loans totaled $5 million and $4 million, respectively.

At September 30, 2013, aggregate restructured loans (accrual, nonaccrual and held-for-sale loans) totaled $349 million, compared to $320 million at December 31, 2012, and $323 million at September 30, 2012. We added $143 million in restructured loans during the first nine months of 2013, which were offset by $114 million in payments and charge-offs.

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A further breakdown of TDRs included in nonperforming loans by loan category as of September 30, 2013, follows:

| **September 30, 2013**<br>*dollars in millions* | **Number of loans** | **Pre-modification Outstanding Recorded Investment** | **Post-modification Outstanding Recorded Investment** |
|---|---|---|---|
| **LOAN TYPE** | | | |
| **Nonperforming:** | | | |
| Commercial, financial and agricultural | 39 | $ 96 | $ 63 |
| Commercial real estate: | | | |
| Real estate commercial mortgage | 14 | 51 | 17 |
| Real estate construction | 6 | 19 | 4 |
| Total commercial real estate loans | 20 | 70 | 21 |
| Total commercial loans | 59 | 166 | 84 |
| Real estate residential mortgage | 401 | 24 | 24 |
| Home equity: | | | |
| Key Community Bank | 1,677 | 89 | 85 |
| Other | 237 | 6 | 6 |
| Total home equity loans | 1,914 | 95 | 91 |
| Consumer other Key Community Bank | 40 | 2 | 1 |
| Credit cards | 689 | 5 | 5 |
| Consumer other: | | | |
| Marine | 346 | 42 | 22 |
| Other | 46 | 1 | 1 |
| Total consumer other | 392 | 43 | 23 |
| Total consumer loans | 3,436 | 169 | 144 |
| Total nonperforming TDRs | 3,495 | 335 | 228 |
| **Prior-year accruing** [(a)] | | | |
| Commercial, financial and agricultural | 68 | 9 | 4 |
| Commercial real estate: | | | |
| Real estate commercial mortgage | 3 | 17 | 12 |
| Real estate construction | 1 | 23 | 35 |
| Total commercial real estate loans | 4 | 40 | 47 |
| Total commercial loans | 72 | 49 | 51 |
| Real estate residential mortgage | 118 | 13 | 13 |
| Home equity: | | | |
| Key Community Bank | 162 | 18 | 17 |
| Other | 214 | 6 | 6 |
| Total home equity loans | 376 | 24 | 23 |
| Consumer other Key Community Bank | 32 | 1 | 1 |
| Credit cards | 267 | 2 | 2 |
| Consumer other: | | | |
| Marine | 276 | 32 | 30 |
| Other | 56 | 1 | 1 |

| | | | | | |
|---|---|---|---|---|---|
| Total consumer other | 332 | | 33 | | 31 |
| Total consumer loans | 1,125 | | 73 | | 70 |
| Total prior-year accruing TDRs | 1,197 | | 122 | | 121 |
| Total TDRs | 4,692 | $ | 457 | $ | 349 |

(a) All TDRs that were restructured prior to January 1, 2013, and are fully accruing.

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A further breakdown of TDRs included in nonperforming loans by loan category as of December 31, 2012, follows:

| **December 31, 2012**<br>*dollars in millions* | **Number of loans** | **Pre-modification Outstanding Recorded Investment** | **Post-modification Outstanding Recorded Investment** |
|---|---|---|---|
| **LOAN TYPE** | | | |
| **Nonperforming:** | | | |
| Commercial, financial and agricultural | 82 | $ 76 | $ 39 |
| Commercial real estate: | | | |
| Real estate commercial mortgage | 15 | 62 | 25 |
| Real estate construction | 8 | 53 | 33 |
| Total commercial real estate loans | 23 | 115 | 58 |
| Total commercial loans | 105 | 191 | 97 |
| Real estate residential mortgage | 372 | 28 | 28 |
| Home equity: | | | |
| Key Community Bank | 1,577 | 87 | 82 |
| Other | 322 | 9 | 8 |
| Total home equity loans | 1,899 | 96 | 90 |
| Consumer other Key Community Bank | 28 | 1 | 1 |
| Credit cards | 405 | 3 | 3 |
| Consumer other: | | | |
| Marine | 251 | 30 | 29 |
| Other | 34 | 1 | 1 |
| Total consumer other | 285 | 31 | 30 |
| Total consumer loans | 2,989 | 159 | 152 |
| Total nonperforming TDRs | 3,094 | 350 | 249 |
| **Prior-year accruing** [(a)] | | | |
| Commercial, financial and agricultural | 122 | 12 | 6 |
| Commercial real estate: | | | |
| Real estate commercial mortgage | 4 | 22 | 15 |
| Total commercial real estate loans | 4 | 22 | 15 |
| Total commercial loans | 126 | 34 | 21 |
| Real estate residential mortgage | 101 | 10 | 10 |
| Home equity: | | | |
| Key Community Bank | 76 | 5 | 5 |
| Other | 84 | 3 | 3 |
| Total home equity loans | 160 | 8 | 8 |
| Consumer other Key Community Bank | 16 | | |
| Consumer other: | | | |
| Marine | 117 | 31 | 31 |
| Other | 43 | 1 | 1 |
| Total consumer other | 160 | 32 | 32 |

| | | | | | |
|---|---|---|---|---|---|
| Total consumer loans | 437 | | 50 | | 50 |
| Total prior-year accruing TDRs | 563 | | 84 | | 71 |
| Total TDRs | 3,657 | $ | 434 | $ | 320 |

(a) All TDRs that were restructured prior to January 1, 2012, and are fully accruing.

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A further breakdown of TDRs included in nonperforming loans by loan category as of September 30, 2012, follows:

| September 30, 2012<br>*dollars in millions* | Number of loans | Pre-modification Outstanding Recorded Investment | Post-modification Outstanding Recorded Investment |
|---|---|---|---|
| **LOAN TYPE** | | | |
| **Nonperforming:** | | | |
| Commercial, financial and agricultural | 91 | $ 107 | $ 54 |
| Commercial real estate: | | | |
| Real estate commercial mortgage | 18 | 47 | 29 |
| Real estate construction | 8 | 53 | 30 |
| Total commercial real estate loans | 26 | 100 | 59 |
| Total commercial loans | 117 | 207 | 113 |
| Real estate residential mortgage | 70 | 7 | 7 |
| Home equity: | | | |
| Key Community Bank | 1,804 | 89 | 58 |
| Other | 486 | 11 | 7 |
| Total home equity loans | 2,290 | 100 | 65 |
| Consumer other Key Community Bank | 125 | 2 | 2 |
| Consumer other: | | | |
| Marine | 491 | 33 | 28 |
| Other | 91 | 2 | 2 |
| Total consumer other | 582 | 35 | 30 |
| Total consumer loans | 3,067 | 144 | 104 |
| Total nonperforming TDRs | 3,184 | 351 | 217 |
| **Prior-year accruing** [(a)] | | | |
| Commercial, financial and agricultural | 152 | 15 | 7 |
| Commercial real estate: | | | |
| Real estate commercial mortgage | 7 | 71 | 45 |
| Real estate construction | 1 | 15 | |
| Total commercial real estate loans | 8 | 86 | 45 |
| Total commercial loans | 160 | 101 | 52 |
| Real estate residential mortgage | 108 | 11 | 11 |
| Home equity: | | | |
| Key Community Bank | 86 | 6 | 6 |
| Other | 95 | 3 | 3 |
| Total home equity loans | 181 | 9 | 9 |
| Consumer other Key Community Bank | 20 | | |
| Consumer other: | | | |
| Marine | 126 | 32 | 32 |
| Other | 51 | 2 | 2 |
| Total consumer other | 177 | 34 | 34 |

| | | | | | |
|---|---|---|---|---|---|
| Total consumer loans | 486 | | 54 | | 54 |
| Total prior-year accruing TDRs | 646 | | 155 | | 106 |
| Total TDRs | 3,830 | $ | 506 | $ | 323 |

(a) All TDRs that were restructured prior to January 1, 2012, and are fully accruing.

We classify loan modifications as TDRs when a borrower is experiencing financial difficulties and we have granted a concession to the borrower without commensurate financial, structural, or legal consideration. All commercial and consumer loan TDRs, regardless of size, are evaluated for impairment individually to determine the probable loss content and are assigned a specific loan allowance if deemed appropriate. The financial effects of TDRs are reflected in the components that make up the allowance for loan and lease losses in either the amount of a charge-off or the 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. There were 138 consumer loan TDRs with a combined recorded investment of $7 million that have experienced payment defaults during the three months ended September 30, 2013 compared to 127 consumer TDRs with a combined recorded investment of $5 million during the three months ended June 30, 2013 from modifications resulting in TDR status during 2012. There were no significant payment defaults during the first nine months of 2013 arising from commercial loans that were designated as TDRs during 2012.

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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 our client s financial needs. Our concession types are primarily interest rate reductions, forgiveness of principal and other modifications. Other loan term modifications for consumer TDRs include concessions determined to have been made as defined in updated regulatory guidance issued in the third quarter of 2012.

The following table shows the concession types for our commercial and consumer accruing and nonaccruing TDRs and other selected financial data.

| *dollars in millions* | **September 30, 2013** | December 31, 2012 | September 30, 2012 |
|---|---|---|---|
| **Commercial loans:** | | | |
| Interest rate reduction | **$ 104** | $ 104 | $ 145 |
| Forgiveness of principal | **5** | 7 | 7 |
| Other modification of loan terms | **26** | 7 | 14 |
| Total | **$ 135** | $ 118 | $ 166 |
| **Consumer loans:** | | | |
| Interest rate reduction | **$ 110** | $ 122 | $ 92 |
| Forgiveness of principal | **5** | 6 | 7 |
| Other modification of loan terms | **99** | 74 | 58 |
| Total | **$ 214** | $ 202 | $ 157 |
| Total commercial and consumer TDRs [a] | **$ 349** | $ 320 | $ 323 |
| Total loans | **53,597** | 52,822 | 51,419 |

(a) Commitments outstanding to lend additional funds to borrowers whose terms have been modified in TDRs are $26 million, $32 million, and $47 million at September 30, 2013, December 31, 2012, and September 30, 2012, 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 on page 120 of our 2012 Form 10-K. Pursuant to regulatory guidance issued in January 2012, the above-mentioned policy for nonperforming loans was revised effective for the second quarter of 2012. Beginning in the second quarter of 2012, any second lien home equity loan with an associated first lien that is 120 days or more past due or in foreclosure or for which the first mortgage delinquency timeframe is unknown, is reported as a nonperforming loan. This policy was implemented prospectively, and, therefore, prior periods were not restated or represented. As of September 30, 2013, in order to be consistent with other unsecured product treatment, the credit card loans nonaccrual policy was revised from 90 day past due status to placement on nonaccrual (and charge off) at 180 days past due.

At September 30, 2013, approximately $52.7 billion, or 98.3%, of our total loans are current. At September 30, 2013, total past due loans and nonperforming loans of $919 million represent approximately 1.7% of total loans.

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The following aging analysis as of September 30, 2013, December 31, 2012, and September 30, 2012, of past due and current loans provides further information regarding Key s credit exposure.

| September 30, 2013<br>*in millions* | Current | 30-59 Days Past Due | 60-89 Days Past Due | 90 and Greater Days Past Due | Nonperforming Loans | Total Past Due and Nonperforming Loans | Purchased Credit Impaired | Total Loans |
|---|---|---|---|---|---|---|---|---|
| **LOAN TYPE** | | | | | | | | |
| Commercial, financial and agricultural | $ 24,161 | $ 33 | $ 9 | $ 12 | $ 102 | $ 156 | | $ 24,317 |
| Commercial real estate: | | | | | | | | |
| Commercial mortgage | 7,429 | 22 | 2 | 31 | 58 | 113 | $ 2 | 7,544 |
| Construction | 1,038 | 3 | | | 17 | 20 | | 1,058 |
| Total commercial real estate loans | 8,467 | 25 | 2 | 31 | 75 | 133 | 2 | 8,602 |
| Commercial lease financing | 4,472 | 41 | 7 | 8 | 22 | 78 | | 4,550 |
| Total commercial loans | $ 37,100 | $ 99 | $ 18 | $ 51 | $ 199 | $ 367 | $ 2 | $ 37,469 |
| Real estate residential mortgage | $ 2,045 | $ 22 | $ 9 | $ 10 | $ 98 | $ 139 | $ 14 | $ 2,198 |
| Home equity: | | | | | | | | |
| Key Community Bank | 9,994 | 50 | 29 | 12 | 198 | 289 | 2 | 10,285 |
| Other | 327 | 8 | 3 | 2 | 13 | 26 | | 353 |
| Total home equity loans | 10,321 | 58 | 32 | 14 | 211 | 315 | 2 | 10,638 |
| Consumer other Key Community Bank | 1,419 | 8 | 5 | 6 | 2 | 21 | | 1,440 |
| Credit cards | 675 | 7 | 4 | 8 | 4 | 23 | | 698 |
| Consumer other: | | | | | | | | |
| Marine | 1,034 | 17 | 6 | 1 | 25 | 49 | | 1,083 |
| Other | 66 | 2 | 1 | | 2 | 5 | | 71 |
| Total consumer other | 1,100 | 19 | 7 | 1 | 27 | 54 | | 1,154 |
| Total consumer loans | $ 15,560 | $ 114 | $ 57 | $ 39 | $ 342 | $ 552 | $ 16 | $ 16,128 |
| Total loans | $ 52,660 | $ 213 | $ 75 | $ 90 | $ 541 | $ 919 | $ 18 | $ 53,597 |

| December 31, 2012<br>*in millions* | Current | 30-59 Days Past Due | 60-89 Days Past Due | 90 and Greater Days Past Due | Nonperforming Loans [(a)] | Total Past Due and Nonperforming Loans | Purchased Credit Impaired | Total Loans |
|---|---|---|---|---|---|---|---|---|
| **LOAN TYPE** | | | | | | | | |
| Commercial, financial and agricultural | $ 23,030 | $ 56 | $ 34 | $ 22 | $ 99 | $ 211 | $ 1 | $ 23,242 |
| Commercial real estate: | | | | | | | | |
| Commercial mortgage | 7,556 | 21 | 11 | 9 | 120 | 161 | 3 | 7,720 |
| Construction | 943 | 1 | 2 | 1 | 56 | 60 | | 1,003 |
| Total commercial real estate loans | 8,499 | 22 | 13 | 10 | 176 | 221 | 3 | 8,723 |
| Commercial lease financing | 4,772 | 88 | 31 | 8 | 16 | 143 | | 4,915 |
| Total commercial loans | $ 36,301 | $ 166 | $ 78 | $ 40 | $ 291 | $ 575 | $ 4 | $ 36,880 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Real estate residential mortgage | $ 2,023 | $ 16 | $ 10 | $ 6 | $ 103 | $ 135 | $ 16 | $ 2,174 |
| Home equity: | | | | | | | | |
| Key Community Bank | 9,506 | 54 | 26 | 17 | 210 | 307 | 3 | 9,816 |
| Other | 387 | 9 | 4 | 2 | 21 | 36 | | 423 |
| Total home equity loans | 9,893 | 63 | 30 | 19 | 231 | 343 | 3 | 10,239 |
| Consumer other Key Community Bank | 1,325 | 9 | 5 | 8 | 2 | 24 | | 1,349 |
| Credit cards | 706 | 7 | 5 | | 11 | 23 | | 729 |
| Consumer other: | | | | | | | | |
| Marine | 1,288 | 23 | 9 | 4 | 34 | 70 | | 1,358 |
| Other | 87 | 2 | 1 | 1 | 2 | 6 | | 93 |
| Total consumer other | 1,375 | 25 | 10 | 5 | 36 | 76 | | 1,451 |
| Total consumer loans | $ 15,322 | $ 120 | $ 60 | $ 38 | $ 383 | $ 601 | $ 19 | $ 15,942 |
| Total loans | $ 51,623 | $ 286 | $ 138 | $ 78 | $ 674 | $ 1,176 | $ 23 | $ 52,822 |

(a) Includes $72 million of performing secured loans that were discharged through Chapter 7 bankruptcy and not formally re-affirmed as addressed in updated regulatory guidance issued in the third quarter of 2012. Such loans have been designated as nonperforming and TDRs.

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| September 30, 2012 in millions | Current | 30-59 Days Past Due | 60-89 Days Past Due | 90 and Greater Days Past Due | Nonperforming Loans [(a)] | Total Past Due and Nonperforming Loans | Purchased Credit Impaired | Total Loans |
|---|---|---|---|---|---|---|---|---|
| **LOAN TYPE** | | | | | | | | |
| Commercial, financial and agricultural | $ 21,766 | $ 46 | $ 19 | $ 15 | $ 132 | $ 212 | $ 1 | $ 21,979 |
| Commercial real estate: | | | | | | | | |
| Commercial mortgage | 7,344 | 19 | 3 | 26 | 134 | 182 | 3 | 7,529 |
| Construction | 993 | 5 | 3 | 13 | 53 | 74 | | 1,067 |
| Total commercial real estate loans | 8,337 | 24 | 6 | 39 | 187 | 256 | 3 | 8,596 |
| Commercial lease financing | 4,881 | 48 | 11 | 2 | 18 | 79 | | 4,960 |
| Total commercial loans | $ 34,984 | $ 118 | $ 36 | $ 56 | $ 337 | $ 547 | $ 4 | $ 35,535 |
| Real estate residential mortgage | $ 1,997 | $ 22 | $ 13 | $ 6 | $ 83 | $ 124 | $ 17 | $ 2,138 |
| Home equity: | | | | | | | | |
| Key Community Bank | 9,492 | 57 | 30 | 15 | 171 | 273 | 3 | 9,768 |
| Other | 374 | 9 | 5 | 3 | 18 | 35 | | 409 |
| Total home equity loans | 9,866 | 66 | 35 | 18 | 189 | 308 | 3 | 10,177 |
| Consumer other Key Community Bank | 1,290 | 9 | 4 | 6 | 3 | 22 | 1 | 1,313 |
| Credit cards | 692 | 6 | 4 | | 8 | 18 | | 710 |
| Consumer other: | | | | | | | | |
| Marine | 1,377 | 29 | 9 | 2 | 31 | 71 | | 1,448 |
| Other | 92 | 2 | 1 | 1 | 2 | 6 | | 98 |
| Total consumer other | 1,469 | 31 | 10 | 3 | 33 | 77 | | 1,546 |
| Total consumer loans | $ 15,314 | $ 134 | $ 66 | $ 33 | $ 316 | $ 549 | $ 21 | $ 15,884 |
| Total loans | $ 50,298 | $ 252 | $ 102 | $ 89 | $ 653 | $ 1,096 | $ 25 | $ 51,419 |

(a) Includes $38 million of performing secured loans that were discharged through Chapter 7 bankruptcy and not formally re-affirmed as addressed in updated regulatory guidance issued in the third quarter of 2012. Such loans have been designated as nonperforming and TDRs.

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 assigned loan risk rating grades for the commercial loan portfolios and the regulatory risk ratings assigned for the consumer loan portfolios. This risk rating stratification assists in the determination of the ALLL. Loan grades are assigned at the time of origination, verified by credit risk management, and periodically reevaluated thereafter.

Most extensions of credit are subject to loan grading or scoring. 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 within the context of the general economic outlook. Types of exposure, transaction structure, and collateral, including credit risk mitigants, affect the expected recovery assessment.

Credit quality indicators for loans are updated on an ongoing basis. Bond rating classifications are indicative of the credit quality of our commercial loan portfolios and are determined by converting our internally assigned risk rating grades to bond rating categories. Payment activity and the regulatory classifications of pass and substandard are indicators of the credit quality of our consumer loan portfolios.

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Credit quality indicators for our commercial and consumer loan portfolios, excluding $18 million of PCI loans at September 30, 2013, based on bond rating, regulatory classification and payment activity as of September 30, 2013, and 2012 are as follows:

**Commercial Credit Exposure**

**Credit Risk Profile by Creditworthiness Category [(a)]**

**September 30,**

*in millions*

| **RATING [(b) (c)]** | **Commercial, financial and agricultural 2013** | **2012** | **RE Commercial 2013** | **2012** | **RE Construction 2013** | **2012** | **Commercial Lease 2013** | **2012** | **Total 2013** | **2012** |
|---|---|---|---|---|---|---|---|---|---|---|
| AAA AA | **$ 292** | $ 166 | | $ 1 | **$ 1** | $ 1 | **$ 454** | $ 465 | **$ 747** | $ 633 |
| A | **774** | 755 | **$ 73** | 63 | **1** | 1 | **866** | 1,107 | **1,714** | 1,926 |
| BBB BB | **21,837** | 19,229 | **6,867** | 6,137 | **879** | 759 | **3,021** | 3,087 | **32,604** | 29,212 |
| B | **487** | 940 | **294** | 585 | **26** | 38 | **133** | 188 | **940** | 1,751 |
| CCC C | **927** | 888 | **308** | 740 | **151** | 268 | **76** | 113 | **1,462** | 2,009 |
| Total | **$ 24,317** | $ 21,978 | **$ 7,542** | $ 7,526 | **$ 1,058** | $ 1,067 | **$ 4,550** | $ 4,960 | **$ 37,467** | $ 35,531 |

(a) Credit quality indicators are updated on an ongoing basis and reflect credit quality information as of the dates indicated.
(b) Our bond rating to internal loan grade conversion system is as follows: AAA - AA = 1, A = 2, BBB - BB = 3 - 13, B = 14 - 16, and CCC - C = 17 - 20.
(c) Our internal loan grade to regulatory-defined classification is as follows: Pass = 1-16, Special Mention = 17, Substandard = 18, Doubtful = 19, and Loss = 20.

**Consumer Credit Exposure**

**Credit Risk Profile by Regulatory Classifications [(a) (b)]**

**September 30,**

*in millions*

| **GRADE** | **Residential Prime 2013** | **2012** |
|---|---|---|
| Pass | **$ 12,487** | $ 11,999 |
| Substandard | **333** | 296 |
| Total | **$ 12,820** | $ 12,295 |

**Credit Risk Profile Based on Payment Activity [(a) (b)]**

| **September 30,** *in millions* | **Consumer Key Community Bank 2013** | **2012** | **Credit cards 2013** | **2012** | **Consumer Marine 2013** | **2012** | **Consumer Other 2013** | **2012** | **Total 2013** | **2012** |
|---|---|---|---|---|---|---|---|---|---|---|
| Performing | **$ 1,438** | $ 1,309 | **$ 694** | $ 702 | **$ 1,058** | $ 1,417 | **$ 69** | $ 96 | **$ 3,259** | $ 3,524 |
| Nonperforming | **2** | 3 | **4** | 8 | **25** | 31 | **2** | 2 | **33** | 44 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Total | **$ 1,440** | $ 1,312 | **$ 698** | $ 710 | **$ 1,083** | $ 1,448 | **$ 71** | $ 98 | **$ 3,292** | $ 3,568 |

(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. Beginning in the second quarter of 2012, any second lien home equity loan with an associated first lien that is 120 days or more past due or in foreclosure or for which the first mortgage delinquency timeframe is unknown, is reported as a nonperforming loan in accordance with regulatory guidance issued in January 2012.

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 on page 120 of our 2012 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 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 greater than $2.5 million, we conduct further analysis to determine the probable loss content and assign a specific allowance to the loan if deemed appropriate. We estimate the extent of impairment 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. 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 September 30, 2013, represents our best estimate of the probable credit losses inherent in the loan portfolio at that date.

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Although quantitative modeling factors such as default probability and expected recovery rates are constantly changing as the financial strength of the borrower and overall economic conditions change, there have been no changes to the accounting policies or methodology we used to estimate the ALLL.

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. Home equity and residential mortgage loans generally are charged down to the fair value of the underlying collateral when payment is 180 days past due. Credit card loans are charged off when payments are 180 days past due. All other consumer loans are charged off when payments are 120 days past due.

At September 30, 2013, the ALLL was $868 million, or 1.62% of loans, compared to $888 million, or 1.73% of loans, at September 30, 2012. At September 30, 2013, the ALLL was 160.4% of nonperforming loans, compared to 136.0% at September 30, 2012.

A summary of the allowance for loan and lease losses for the periods indicated is presented in the table below:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| *in millions* | **2013** | **2012** | **2013** | **2012** |
| Balance at beginning of period continuing operations | **$ 876** | $ 888 | **$ 888** | $ 1,004 |
| Charge-offs | **(78)** | (141) | **(242)** | (404) |
| Recoveries | **41** | 32 | **111** | 117 |
| Net loans and leases charged off | **(37)** | (109) | **(131)** | (287) |
| Provision for loan and lease losses from continuing operations | **28** | 109 | **111** | 172 |
| Foreign currency translation adjustment | **1** | | | (1) |
| Balance at end of period continuing operations | **$ 868** | $ 888 | **$ 868** | $ 888 |

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

| *in millions* | December 31, 2012 | Provision | Charge-offs | Recoveries | September 30, 2013 |
|---|---|---|---|---|---|
| Commercial, financial and agricultural | $ 327 | **$ 57** | **$ (44)** | **$ 30** | **$ 370** |
| Real estate commercial mortgage | 198 | **(28)** | **(18)** | **20** | **172** |
| Real estate construction | 41 | **(17)** | **(2)** | **14** | **36** |
| Commercial lease financing | 55 | **24** | **(25)** | **10** | **64** |
| Total commercial loans | 621 | **36** | **(89)** | **74** | **642** |
| Real estate residential mortgage | 30 | **17** | **(13)** | **1** | **35** |
| Home equity: | | | | | |
| Key Community Bank | 105 | **19** | **(50)** | **8** | **82** |
| Other | 25 | | **(16)** | **5** | **14** |
| Total home equity loans | 130 | **19** | **(66)** | **13** | **96** |
| Consumer other Key Community Bank | 38 | **8** | **(24)** | **5** | **27** |
| Credit cards | 26 | **30** | **(25)** | **3** | **34** |
| Consumer other: | | | | | |
| Marine | 39 | **1** | **(22)** | **13** | **31** |
| Other | 4 | | **(3)** | **2** | **3** |
| Total consumer other: | 43 | **1** | **(25)** | **15** | **34** |
| Total consumer loans | 267 | **75** | **(153)** | **37** | **226** |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Total ALLL continuing operations | | 888 | | **111** | | **(242)** | | **111** | **868** |
| Discontinued operations | | 55 | | **11** | | **(42)** | | **14** | **38** |
| Total ALLL including discontinued operations | $ | 943 | **$** | **122** | **$** | **(284)** | **$** | **125** | **$ 906** |

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| *in millions* | December 31, 2011 | Provision | Charge-offs | Recoveries | September 30, 2012 |
|---|---|---|---|---|---|
| Commercial, financial and agricultural | $ 334 | $ 9 | $ (65) | $ 40 | $ 318 |
| Real estate commercial mortgage | 272 | | (69) | 18 | 221 |
| Real estate construction | 63 | | (19) | 3 | 47 |
| Commercial lease financing | 78 | (10) | (20) | 18 | 66 |
| Total commercial loans | 747 | (1) | (173) | 79 | 652 |
| Real estate residential mortgage | 37 | 5 | (19) | 2 | 25 |
| Home equity: | | | | | |
| Key Community Bank | 103 | 92 | (113) | 7 | 89 |
| Other | 29 | 14 | (23) | 4 | 24 |
| Total home equity loans | 132 | 106 | (136) | 11 | 113 |
| Consumer other Key Community Bank | 41 | 15 | (29) | 5 | 32 |
| Credit cards | | 27 | (2) | | 25 |
| Consumer other: | | | | | |
| Marine | 46 | 14 | (41) | 18 | 37 |
| Other | 1 | 5 | (4) | 2 | 4 |
| Total consumer other: | 47 | 19 | (45) | 20 | 41 |
| Total consumer loans | 257 | 172 | (231) | 38 | 236 |
| Total ALLL continuing operations | 1,004 | 171 [(a)] | (404) | 117 | 888 |
| Discontinued operations | 104 | 4 | (56) | 13 | 65 |
| Total ALLL including discontinued operations | $ 1,108 | $ 175 | $ (460) | $ 130 | $ 953 |

(a) Includes $1 million of foreign currency translation adjustment.

Our ALLL decreased by $20 million, or 2%, since the third quarter of 2012. This contraction was associated with the improvement in credit quality of our loan portfolios. The quality of new loan originations and decreasing NPLs and net charge-offs has resulted in a reduction in our general allowance. Our general allowance encompasses the application of expected loss rates to our existing loans with similar risk characteristics, an assessment of factors such as changes in economic conditions and changes in credit policies or underwriting standards. Our delinquency trends have declined during 2012 and thus far in 2013 due to a modest level of loan growth, relatively stable conditions in the economic environment, and continued run off in our exit loan portfolio and reflects our effort to maintain a moderate enterprise risk tolerance.

For continuing operations, the loans outstanding individually evaluated for impairment totaled $411 million, with a corresponding allowance of $47 million at September 30, 2013. Loans outstanding collectively evaluated for impairment totaled $53.2 billion, with a corresponding allowance of $820 million at September 30, 2013. At September 30, 2013, PCI loans evaluated for impairment totaled $18 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 September 30, 2013.

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A breakdown of the individual and collective ALLL and the corresponding loan balances as of September 30, 2013, follows:

| September 30, 2013 | Allowance | | | Outstanding | | | |
|---|---|---|---|---|---|---|---|
| *in millions* | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Purchased Credit Impaired | Loans | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Purchased Credit Impaired |
| Commercial, financial and agricultural | $ 17 | $ 353 | | $ 24,317 | $ 108 | $ 24,209 | |
| Commercial real estate: | | | | | | | |
| Commercial mortgage | 1 | 171 | | 7,544 | 46 | 7,496 | $ 2 |
| Construction | | 36 | | 1,058 | 44 | 1,014 | |
| Total commercial real estate loans | 1 | 207 | | 8,602 | 90 | 8,510 | 2 |
| Commercial lease financing | | 64 | | 4,550 | | 4,550 | |
| Total commercial loans | 18 | 624 | | 37,469 | 198 | 37,269 | 2 |
| Real estate residential mortgage | 6 | 28 | $ 1 | 2,198 | 36 | 2,148 | 14 |
| Home equity: | | | | | | | |
| Key Community Bank | 10 | 72 | | 10,285 | 102 | 10,181 | 2 |
| Other | 2 | 12 | | 353 | 13 | 340 | |
| Total home equity loans | 12 | 84 | | 10,638 | 115 | 10,521 | 2 |
| Consumer other Key Community Bank | | 27 | | 1,440 | 3 | 1,437 | |
| Credit cards | 1 | 33 | | 698 | 6 | 692 | |
| Consumer other: | | | | | | | |
| Marine | 10 | 21 | | 1,083 | 52 | 1,031 | |
| Other | | 3 | | 71 | 1 | 70 | |
| Total consumer other | 10 | 24 | | 1,154 | 53 | 1,101 | |
| Total consumer loans | 29 | 196 | 1 | 16,128 | 213 | 15,899 | 16 |
| Total ALLL continuing operations | 47 | 820 | 1 | 53,597 | 411 | 53,168 | 18 |
| Discontinued operations | 1 | 37 | | 4,738 [(a)] | 11 | 4,727 | |
| Total ALLL including discontinued operations | $ 48 | $ 857 | $ 1 | $ 58,335 | $ 422 | $ 57,895 | $ 18 |

(a) Amount includes $2.3 billion 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, 2012, follows:

| December 31, 2012 | Allowance | | | Outstanding | | | |
|---|---|---|---|---|---|---|---|
| *in millions* | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Purchased Credit Impaired | Loans | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Purchased Credit Impaired |
| Commercial, financial and agricultural | $ 12 | $ 314 | | $ 23,242 | $ 65 | $ 23,176 | $ 1 |
| Commercial real estate: | | | | | | | |
| Commercial mortgage | 1 | 198 | | 7,720 | 96 | 7,621 | 3 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Construction | | 41 | | 1,003 | 48 | 955 | |
| Total commercial real estate loans | 1 | 239 | | 8,723 | 144 | 8,576 | 3 |
| Commercial lease financing | | 55 | | 4,915 | | 4,915 | |
| Total commercial loans | 13 | 608 | | 36,880 | 209 | 36,667 | 4 |
| Real estate residential mortgage | 1 | 29 | $ 1 | 2,174 | 38 | 2,120 | 16 |
| Home equity: | | | | | | | |
| Key Community Bank | 11 | 94 | | 9,816 | 87 | 9,726 | 3 |
| Other | 1 | 24 | | 423 | 12 | 411 | |
| Total home equity loans | 12 | 118 | | 10,239 | 99 | 10,137 | 3 |
| Consumer other Key Community Bank | 2 | 36 | | 1,349 | 2 | 1,347 | |
| Credit cards | | 26 | | 729 | 2 | 727 | |
| Consumer other: | | | | | | | |
| Marine | 7 | 32 | | 1,358 | 60 | 1,298 | |
| Other | | 3 | | 93 | 1 | 92 | |
| Total consumer other | 7 | 35 | | 1,451 | 61 | 1,390 | |
| Total consumer loans | 22 | 244 | 1 | 15,942 | 202 | 15,721 | 19 |
| Total ALLL continuing operations | 35 | 852 | 1 | 52,822 | 411 | 52,388 | 23 |
| Discontinued operations | | 55 | | 5,201 [a] | 3 | 5,198 | |
| Total ALLL including discontinued operations | $ 35 | $ 907 | $ 1 | $ 58,023 | $ 414 | $ 57,586 | $ 23 |

(a) Amount includes $2.5 billion 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 September 30, 2012, follows:

| September 30, 2012 | Allowance | | | | Outstanding | | |
|---|---|---|---|---|---|---|---|
| *in millions* | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Purchased Credit Impaired | Loans | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Purchased Credit Impaired |
| Commercial, financial and agricultural | $ 12 | $ 306 | | $ 21,979 | $ 92 | $ 21,886 | $ 1 |
| Commercial real estate: | | | | | | | |
| Commercial mortgage | 7 | 214 | | 7,529 | 138 | 7,388 | 3 |
| Construction | | 47 | | 1,067 | 42 | 1,025 | |
| Total commercial real estate loans | 7 | 261 | | 8,596 | 180 | 8,413 | 3 |
| Commercial lease financing | | 66 | | 4,960 | | 4,960 | |
| Total commercial loans | 19 | 633 | | 35,535 | 272 | 35,259 | 4 |
| Real estate residential mortgage | 1 | 24 | | 2,138 | 18 | 2,103 | 17 |
| Home equity: | | | | | | | |
| Key Community Bank | 10 | 79 | | 9,768 | 65 | 9,700 | 3 |
| Other | 1 | 23 | | 409 | 10 | 399 | |
| Total home equity loans | 11 | 102 | | 10,177 | 75 | 10,099 | 3 |
| Consumer other Key Community Bank | 1 | 31 | | 1,313 | 2 | 1,310 | 1 |
| Credit cards | | 25 | | 710 | | 710 | |
| Consumer other: | | | | | | | |
| Marine | 7 | 30 | | 1,448 | 60 | 1,388 | |
| Other | | 4 | | 98 | 1 | 97 | |
| Total consumer other | 7 | 34 | | 1,546 | 61 | 1,485 | |
| Total consumer loans | 20 | 216 | | 15,884 | 156 | 15,707 | 21 |
| Total ALLL continuing operations | 39 | 849 | | 51,419 | 428 | 50,966 | 25 |
| Discontinued operations | | 65 | | 5,328 (a) | 3 | 5,325 | |
| Total ALLL including discontinued operations | $ 39 | $ 914 | | $ 56,747 | $ 431 | $ 56,291 | $ 25 |

(a) Amount includes $2.6 billion of loans carried at fair value that are excluded from ALLL considerations.

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 has decreased by $3 million since the third quarter of 2012 to $40 million at September 30, 2013. When combined with our ALLL, our total allowance for credit losses represented 1.69% of loans at September 30, 2013, compared to 1.81% at September 30, 2012.

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

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| *in millions* | **2013** | 2012 | **2013** | 2012 |
| Balance at beginning of period | **$ 37** | $ 51 | **$ 29** | $ 45 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Provision (credit) for losses on lending-related commitments | | **3** | | (8) | | **11** | | (2) |
| Balance at end of period | **$** | **40** | $ | 43 | **$** | **40** | $ | 43 |

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### 5. Fair Value Measurements

**Fair Value Determination**

As defined in the applicable accounting guidance, fair value is the price to sell an asset or 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 for all lines of business and support areas, as applicable. Various Working Groups that report to the Fair Value Committee analyze and approve the valuation methodologies used to fair value assets and liabilities managed within specific areas. The Working Groups are discussed in more detail in the qualitative disclosures within this footnote 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 on page 122 of our 2012 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.

***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 actual trade data (i.e., spreads, credit ratings, and interest rates) for comparable assets, spread tables, matrices, high-grade scales, option-adjusted spreads, and standard inputs, such as yields, benchmark securities, bids, and offers.

Securities are classified as Level 3 when there is limited activity in the market for a particular instrument. In such cases, we use internal models based on certain assumptions to determine fair value. Level 3 instruments consist of certain commercial mortgage-backed securities. Our Real Estate Capital line of business is responsible for the valuation process for these commercial mortgage-backed securities, which is conducted on a quarterly basis. The methodology incorporates a loan-by-loan credit review in combination with discounting the risk-adjusted bond cash flows. A detailed credit review of the underlying loans involves a screening process using a multitude of filters to identify the highest risk loans associated with these commercial mortgage-backed securities. Each of the highest risk loans identified is re-underwritten and loan specific defaults and recoveries are assigned. A matrix approach is used to assign an expected default and recovery percentage for the loans that are not individually re-underwritten. Bond classes will then be run through a discounted cash flow analysis, taking into account the expected default and recovery percentages as well as discount rates developed by our Finance area. Inputs for the Level 3 internal models include expected cash flows from the underlying loans, which take into account expected default and recovery percentages, market research, and discount rates commensurate with current market conditions. Changes in the credit quality of the underlying loans or market discount rate would impact the value of the bonds. An increase in the underlying loan credit quality or decrease in the market discount rate would positively impact the bond value. A decrease in the underlying loan credit quality or increase in the market discount rate would negatively impact the bond value.

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 state and political subdivisions securities, 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.

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. Periodically, a third-party appraisal is obtained for the

investment to validate the specific inputs for determining fair value.

Inputs used in calculating future cash flows include the cost of build-out, future selling prices, current market outlook, and operating performance of the investment. Investment income and expense assumptions are based on market inputs, such as rental/leasing rates and vacancy rates for the geographic- and property type-specific markets. For investments under construction, investment income and expense assumptions are determined using expected future build-out costs and anticipated future rental prices based on current market conditions, discount rates, holding period, the terminal cap rate and sales commissions paid in the terminal cap year. For investments that are in lease-up or are fully leased, income and expense assumptions are based on the current geographic market lease rates, underwritten expenses, market lease terms, and historical vacancy rates. Asset Management validates these inputs on a quarterly basis through the use of industry publications, third-party broker opinions, and comparable property sales, where applicable. Changes in the significant inputs (rental/leasing rates, vacancy rates, valuation capitalization rate, discount rate, and terminal cap rate) would significantly affect the fair value measurement. Increases in rental/leasing rates would increase fair value while increases in the vacancy rates, the valuation capitalization rate, the discount rate, and the terminal cap rate would decrease fair value.

Indirect investments are valued using a methodology that is consistent with accounting guidance that allows us to use statements from the investment manager to calculate net asset value per share. A primary input used in estimating fair value is 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.

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 September 30, 2013:

**September 30, 2013**

| *in millions* | Fair Value | Unfunded Commitments |
|---|---|---|
| **INVESTMENT TYPE** | | |
| Passive funds [(a)] | $ 13 | $ 1 |
| Co-managed funds [(b)] | 15 | |
| Total | $ 28 | $ 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 seven years.

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

***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), as well as indirect investments (investments made through funds that include other investors).

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 (comprised of individuals from one of the independent investment managers who oversee these instruments), members of the Key Principal Partners ( KPP ) finance and accounting staff, and the Investment Committee (comprised of individuals from 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. However, 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 earnings before interest, taxation, depreciation, and amortization. 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.

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 that is reviewed by the Principal Investing Entities Deal Team Member as well as 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 are classified as Level 3 assets since our significant inputs are not observable in the marketplace. 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). The significant unobservable input used in estimating fair value is primarily the most recent value of the capital accounts as reported by the general partners of the funds in which we invest.

For indirect investments, management makes adjustments as deemed appropriate to the net asset value and only 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. Significant unobservable inputs used in these analyses include current fund financial information provided by the fund manager, an estimate of future proceeds expected to be received on the investment, and market multiples. 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 fair value of our indirect investments and related unfunded commitments at September 30, 2013, was $417 million and $83 million, respectively. Our indirect investments consist of buyout, venture capital, and fund of funds. These investments can never be redeemed. Instead, distributions are received through the liquidation of the underlying investments of the fund. An investment in any one of these funds 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 nine years.

***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 Market Risk Management 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 default reserve. The credit component is determined by individual counterparty based on the probability of default, and considers master netting and collateral agreements. The default reserve is classified as Level 3. Our Market Risk Management group is responsible for the valuation policies and procedure related to this default reserve. 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, Market Risk Management prepares the reserve calculation. A detailed reserve comparison with the previous quarter, an analysis for change in reserve, and a reserve forecast are provided by Market Risk Management to ensure that the default reserve recorded at period end is sufficient.

***Other assets and liabilities***. The value of our repurchase and reverse repurchase agreements, trade date receivables and payables, and short positions is driven by the valuation of the underlying securities. The underlying securities may include equity securities, which are valued using quoted market prices in an active market for identical securities, resulting in a Level 1 classification. 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 September 30, 2013, December 31, 2012 and September 30, 2012.

| **September 30, 2013**<br>*in millions* | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| **ASSETS MEASURED ON A RECURRING BASIS** | | | | |
| Short-term investments: | | | | |
| Securities purchased under resale agreements | | $ 516 | | $ 516 |
| Trading account assets: | | | | |
| U.S. Treasury, agencies and corporations | | 616 | | 616 |
| States and political subdivisions | | 26 | | 26 |
| Collateralized mortgage obligations | | 6 | | 6 |
| Other mortgage-backed securities | | 83 | | 83 |
| Other securities | $ 6 | 66 | | 72 |
| Total trading account securities | 6 | 797 | | 803 |
| Commercial loans | | 3 | | 3 |
| Total trading account assets | 6 | 800 | | 806 |
| Securities available for sale: | | | | |
| States and political subdivisions | | 41 | | 41 |
| Collateralized mortgage obligations | | 11,779 | | 11,779 |
| Other mortgage-backed securities | | 762 | | 762 |
| Other securities | 24 | | | 24 |
| Total securities available for sale | 24 | 12,582 | | 12,606 |
| Other investments: | | | | |
| Principal investments: | | | | |
| Direct | | | $ 168 | 168 |
| Indirect | | | 417 | 417 |
| Total principal investments | | | 585 | 585 |
| Equity and mezzanine investments: | | | | |
| Direct | | | | |
| Indirect | | | 28 | 28 |
| Total equity and mezzanine investments | | | 28 | 28 |
| Total other investments | | | 613 | 613 |
| Derivative assets: | | | | |
| Interest rate | | 1,112 | 19 | 1,131 |
| Foreign exchange | 60 | 10 | | 70 |
| Energy and commodity | | 137 | | 137 |
| Credit | | 2 | 4 | 6 |
| Equity | | | | |
| Derivative assets | 60 | 1,261 | 23 | 1,344 |
| Netting adjustments [(a)] | | | | (869) |
| Total derivative assets | 60 | 1,261 | 23 | 475 |
| Accrued income and other assets | | 48 | | 48 |

| | | | | |
|---|---|---|---|---|
| Total assets on a recurring basis at fair value | $ 90 | $ 15,207 | $ 636 | $ 15,064 |
| **LIABILITIES MEASURED ON A RECURRING BASIS** | | | | |
| Federal funds purchased and securities sold under repurchase agreements: | | | | |
| Securities sold under repurchase agreements | | $ 464 | | $ 464 |
| Bank notes and other short-term borrowings: | | | | |
| Short positions | $ 4 | 458 | | 462 |
| Derivative liabilities: | | | | |
| Interest rate | | 798 | | 798 |
| Foreign exchange | 59 | 10 | | 69 |
| Energy and commodity | | 130 | $ 1 | 131 |
| Credit | | 10 | 1 | 11 |
| Equity | | | | |
| Derivative liabilities | 59 | 948 | 2 | 1,009 |
| Netting adjustments [(a)] | | | | (559) |
| Total derivative liabilities | 59 | 948 | 2 | 450 |
| Accrued expense and other liabilities | | 133 | | 133 |
| Total liabilities on a recurring basis at fair value | $ 63 | $ 2,003 | $ 2 | $ 1,509 |

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

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| **December 31, 2012**<br>*in millions* | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| **ASSETS MEASURED ON A RECURRING BASIS** | | | | |
| Short term investments: | | | | |
| Securities purchased under resale agreements | | $ 271 | | $ 271 |
| Trading account assets: | | | | |
| U.S. Treasury, agencies and corporations | | 383 | | 383 |
| States and political subdivisions | | 21 | $ 3 | 24 |
| Collateralized mortgage obligations | | 8 | | 8 |
| Other mortgage-backed securities | | 4 | | 4 |
| Other securities | $ 2 | 175 | | 177 |
| Total trading account securities | 2 | 591 | 3 | 596 |
| Commercial loans | | 9 | | 9 |
| Total trading account assets | 2 | 600 | 3 | 605 |
| Securities available for sale: | | | | |
| States and political subdivisions | | 49 | | 49 |
| Collateralized mortgage obligations | | 11,464 | | 11,464 |
| Other mortgage-backed securities | | 538 | | 538 |
| Other securities | 43 | | | 43 |
| Total securities available for sale | 43 | 12,051 | | 12,094 |
| Other investments: | | | | |
| Principal investments: | | | | |
| Direct | | | 191 | 191 |
| Indirect | | | 436 | 436 |
| Total principal investments | | | 627 | 627 |
| Equity and mezzanine investments: | | | | |
| Direct | | | | |
| Indirect | | | 41 | 41 |
| Total equity and mezzanine investments | | | 41 | 41 |
| Total other investments | | | 668 | 668 |
| Derivative assets: | | | | |
| Interest rate | | 1,705 | 19 | 1,724 |
| Foreign exchange | 54 | 21 | | 75 |
| Energy and commodity | | 154 | 2 | 156 |
| Credit | | 3 | 5 | 8 |
| Equity | | | | |
| Derivative assets | 54 | 1,883 | 26 | 1,963 |
| Netting adjustments [a] | | | | (1,270) |
| Total derivative assets | 54 | 1,883 | 26 | 693 |
| Accrued income and other assets | | 3 | | 3 |
| Total assets on a recurring basis at fair value | $ 99 | $ 14,808 | $ 697 | $ 14,334 |
| **LIABILITIES MEASURED ON A RECURRING BASIS** | | | | |
| Federal funds purchased and securities sold under repurchase agreements: | | | | |
| Securities sold under repurchase agreements | | $ 228 | | $ 228 |
| Bank notes and other short-term borrowings: | | | | |
| Short positions | | 287 | | 287 |

| | | | | |
|---|---|---|---|---|
| Derivative liabilities: | | | | |
| Interest rate | | 1,152 | | 1,152 |
| Foreign exchange | $ 55 | 20 | | 75 |
| Energy and commodity | | 149 | $ 1 | 150 |
| Credit | | 9 | 1 | 10 |
| Equity | | | | |
| Derivative liabilities | 55 | 1,330 | 2 | 1,387 |
| Netting adjustments [(a)] | | | | (803) |
| Total derivative liabilities | 55 | 1,330 | 2 | 584 |
| Accrued expense and other liabilities | | 49 | | 49 |
| Total liabilities on a recurring basis at fair value | $ 55 | $ 1,894 | $ 2 | $ 1,148 |

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

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| September 30, 2012<br>*in millions* | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **ASSETS MEASURED ON A RECURRING BASIS** | | | | |
| Short term investments: | | | | |
| Securities purchased under resale agreements | | $ 294 | | $ 294 |
| Trading account assets: | | | | |
| U.S. Treasury, agencies and corporations | | 486 | | 486 |
| States and political subdivisions | | 14 | $ 56 | 70 |
| Collateralized mortgage obligations | | 4 | | 4 |
| Other mortgage-backed securities | | 9 | 1 | 10 |
| Other securities | $ 10 | 78 | | 88 |
| Total trading account securities | 10 | 591 | 57 | 658 |
| Commercial loans | | 5 | | 5 |
| Total trading account assets | 10 | 596 | 57 | 663 |
| Securities available for sale: | | | | |
| States and political subdivisions | | 54 | | 54 |
| Collateralized mortgage obligations | | 11,283 | | 11,283 |
| Other mortgage-backed securities | | 597 | 1 | 598 |
| Other securities | 27 | | | 27 |
| Total securities available for sale | 27 | 11,934 | 1 | 11,962 |
| Other investments: | | | | |
| Principal investments: | | | | |
| Direct | | | 214 | 214 |
| Indirect | | | 455 | 455 |
| Total principal investments | | | 669 | 669 |
| Equity and mezzanine investments: | | | | |
| Direct | | | | |
| Indirect | | | 42 | 42 |
| Total equity and mezzanine investments | | | 42 | 42 |
| Total other investments | | | 711 | 711 |
| Derivative assets: | | | | |
| Interest rate | | 1,841 | 23 | 1,864 |
| Foreign exchange | 52 | 29 | | 81 |
| Energy and commodity | | 183 | | 183 |
| Credit | | 14 | 5 | 19 |
| Equity | | | | |
| Derivative assets | 52 | 2,067 | 28 | 2,147 |
| Netting adjustments [(a)] | | | | (1,376) |
| Total derivative assets | 52 | 2,067 | 28 | 771 |
| Accrued income and other assets | | 138 | | 138 |
| Total assets on a recurring basis at fair value | $ 89 | $ 15,029 | $ 797 | $ 14,539 |
| **LIABILITIES MEASURED ON A RECURRING BASIS** | | | | |
| Federal funds purchased and securities sold under repurchase agreements: | | | | |
| Securities sold under repurchase agreements | | $ 398 | | $ 398 |
| Bank notes and other short-term borrowings: | | | | |
| Short positions | $ 4 | 384 | | 388 |

| | | | | |
|---|---|---|---|---|
| Derivative liabilities: | | | | |
| Interest rate | | 1,283 | | 1,283 |
| Foreign exchange | 56 | 27 | | 83 |
| Energy and commodity | | 177 | $ 1 | 178 |
| Credit | | 17 | 1 | 18 |
| Equity | | | | |
| Derivative liabilities | 56 | 1,504 | 2 | 1,562 |
| Netting adjustments [(a)] | | | | (905) |
| Total derivative liabilities | 56 | 1,504 | 2 | 657 |
| Accrued expense and other liabilities | 1 | | | 1 |
| Total liabilities on a recurring basis at fair value | $ 61 | $ 2,286 | $ 2 | $ 1,444 |

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

**Changes in Level 3 Fair Value Measurements**

The following table shows the change in the fair values of our Level 3 financial instruments for the three and nine months ended September 30, 2013, and 2012. We mitigate the credit risk, interest rate risk, and risk of loss related to many of these Level 3 instruments by using securities and derivative positions classified as Level 1 or Level 2. Level 1 and Level 2 instruments are not included in the following table. Therefore, the gains or losses shown do not include the impact of our risk management activities.

| *in millions* | Beginning of Period Balance | Gains (Losses) Included in Earnings | Purchases | Sales | Settlements | Transfers into Level 3 [e] | Transfers out of Level 3 [e] | End of Period Balance [g] | Unrealized Gains (Losses) Included in Earnings |
|---|---|---|---|---|---|---|---|---|---|
| **Nine months ended September 30, 2013** | | | | | | | | | |
| Trading account assets | | | | | | | | | |
| Other mortgage-backed securities | | $ 4 [b] | | $ (4) | | | | | |
| Other securities | | 4 [b] | | | $ (4) | | | | $ (1) [b] |
| State and political subdivisions | $ 3 | | | (3) | | | | | |
| Other investments | | | | | | | | | |
| Principal investments | | | | | | | | | |
| Direct | 191 | (9) [c] | $ 7 | (21) | | | | $ 168 | (19) [c] |
| Indirect | 436 | 37 [c] | 14 | (70) | | | | 417 | 13 [c] |
| Equity and mezzanine investments | | | | | | | | | |
| Direct | | | | | | | | | 8 [c] |
| Indirect | 41 | 1 [c] | | | (14) | | | 28 | 1 [c] |
| Derivative instruments [a] | | | | | | | | | |
| Interest rate | 19 | (10) [d] | | (1) | | $ 39 [f] | $ (28) [f] | 19 | |
| Energy and commodity | 1 | (2) [d] | | | | | | (1) | |
| Credit | 4 | (6) [d] | | | 5 | | | 3 | |
| **Three months ended September 30, 2013** | | | | | | | | | |
| Trading account assets | | | | | | | | | |
| Other mortgage-backed securities | | | | | | | | | |
| Other securities | | $ 1 [b] | | | $ (1) | | | | $ (2) [b] |
| State and political subdivisions | | | | | | | | | |
| Other investments | | | | | | | | | |
| Principal investments | | | | | | | | | |
| Direct | $ 186 | (4) [c] | $ 3 | $ (17) | | | | $ 168 | (8) [c] |
| Indirect | 426 | 18 [c] | 3 | (30) | | | | 417 | 9 [c] |
| Equity and mezzanine investments | | | | | | | | | |
| Direct | | | | | | | | | 5 [c] |
| Indirect | 32 | (1) [c] | | | (3) | | | 28 | (1) [c] |
| Derivative instruments [a] | | | | | | | | | |
| Interest rate | 25 | (7) [d] | | | | | $ 1 [f] | 19 | |
| Energy and commodity | 1 | (2) [d] | | | | | | (1) | |
| Credit | 4 | (3) [d] | | | 2 | | | 3 | |

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| *in millions* | Beginning of Period Balance | Gains (Losses) Included in Earnings | Purchases | Sales | Settlements | Transfers into Level 3 [e] | Transfers out of Level 3 [e] | End of Period Balance [g] | Unrealized Gains (Losses) Included in Earnings |
|---|---|---|---|---|---|---|---|---|---|
| **Nine months ended September 30, 2012** | | | | | | | | | |
| Trading account assets | | | | | | | | | |
| Other mortgage-backed securities | $ 35 | $ 2 [b] | | $ (32) | | | $ (4) | $ 1 | |
| Other securities | | 2 [b] | | | $ (3) | $ 57 [h] | | 56 | $ 2 [b] |
| Other investments | | | | | | | | | |
| Principal investments | | | | | | | | | |
| Direct | 225 | 12 [c] | $ 11 | (34) | | | | 214 | 10 [c] |
| Indirect | 473 | 50 [c] | 24 | (92) | | | | 455 | 21 [c] |
| Equity and mezzanine investments | | | | | | | | | |
| Direct | 15 | 3 [c] | | | (18) | | | | 15 [c] |
| Indirect | 36 | 6 [c] | 4 | | (4) | | | 42 | 6 [c] |
| Derivative instruments [a] | | | | | | | | | |
| Interest rate | 38 | (5) [d] | 1 | (7) | | 7 | (11) | 23 | |
| Energy and commodity | (1) | 1 [d] | (1) | | | | | (1) | |
| Credit | (21) | (11) [d] | | | 37 | | | 5 | |
| **Three months ended September 30, 2012** | | | | | | | | | |
| Trading account assets | | | | | | | | | |
| Other mortgage-backed securities | $ 1 | | | | | | | $ 1 | |
| Other securities | 57 | $ 4 [b] | | | $ (5) | | | 56 | $ 4 [b] |
| Other investments | | | | | | | | | |
| Principal investments | | | | | | | | | |
| Direct | 231 | 4 [c] | $ 1 | $ (22) | | | | 214 | 2 [c] |
| Indirect | 482 | 7 [c] | 4 | (38) | | | | 455 | (7) [c] |
| Equity and mezzanine investments | | | | | | | | | |
| Direct | 18 | | | | (18) | | | | 5 [c] |
| Indirect | 43 | | | | | $ (1) | | 42 | |
| Derivative instruments [a] | | | | | | | | | |
| Interest rate | 35 | (2) [d] | | (6) | | 3 | $ (7) | 23 | |
| Energy and commodity | (1) | | | | | | | (1) | |
| Credit | 5 | (4) [d] | | | 4 | | | 5 | |

(a) Amounts represent Level 3 derivative assets less Level 3 derivative liabilities.

(b) Realized and unrealized gains and losses on trading account assets are reported in other income on the income statement.

(c) Realized and unrealized gains and losses on principal investments and private equity and mezzanine investments are reported in net gains (losses) from principal investing on the income statement.

(d) Realized and unrealized gains and losses on derivative instruments are reported in corporate services income and other income on the income statement.

(e) Our policy is to recognize transfers into and transfers out of Level 3 as of the end of the reporting period.

(f) Transfers from Level 2 to Level 3 were the result of Level 3 unobservable inputs becoming significant to certain derivatives previously classified as Level 2. Transfers from Level 3 to Level 2 were the result of Level 3 unobservable inputs becoming less significant to certain derivatives previously classified as Level 3.

(g) There were no issuances for the nine-month periods ended September 30, 2013 and 2012.
(h) Transfers from Level 2 to Level 3 were the result of decreased observable market activity for these securities.

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**Assets Measured at Fair Value on a Nonrecurring Basis**

Certain assets and liabilities are measured at fair value on a nonrecurring basis in accordance with GAAP. The adjustments to fair value generally result from the application of accounting guidance that requires assets and liabilities to be recorded at the lower of cost or fair value, or assessed for impairment. The following table presents our assets measured at fair value on a nonrecurring basis at September 30, 2013, December 31, 2012, and September 30, 2012:

| | September 30, 2013 | | | |
|---|---|---|---|---|
| *in millions* | Level 1 | Level 2 | Level 3 | Total |
| **ASSETS MEASURED ON A NONRECURRING BASIS** | | | | |
| Impaired loans | | | **$ 26** | **$ 26** |
| Loans held for sale [(a)] | | | | |
| Accrued income and other assets | | **$ 1** | **10** | **11** |
| Total assets on a nonrecurring basis at fair value | | **1** | **$ 36** | **$ 37** |

| | December 31, 2012 | | | |
|---|---|---|---|---|
| *in millions* | Level 1 | Level 2 | Level 3 | Total |
| **ASSETS MEASURED ON A NONRECURRING BASIS** | | | | |
| Impaired loans | | | $ 25 | $ 25 |
| Loans held for sale [(a)] | | | 9 | 9 |
| Accrued income and other assets | | $ 2 | 20 | 22 |
| Total assets on a nonrecurring basis at fair value | | $ 2 | $ 54 | $ 56 |

| | September 30, 2012 | | | |
|---|---|---|---|---|
| *in millions* | Level 1 | Level 2 | Level 3 | Total |
| **ASSETS MEASURED ON A NONRECURRING BASIS** | | | | |
| Impaired loans | | | $ 52 | $ 52 |
| Loans held for sale [(a)] | | | 10 | 10 |
| Accrued income and other assets | | $ 15 | 22 | 37 |
| Total assets on a nonrecurring basis at fair value | | $ 15 | $ 84 | $ 99 |

(a) During the first nine months of 2013, we transferred $2 million of commercial and consumer loans and leases at their current fair value from held-for-sale status to the held-to-maturity portfolio compared to $17 million during 2012, and $17 million during the first nine months ended September 30, 2012.

***Impaired loans***. We typically adjust the carrying amount of our impaired loans when there is evidence of probable loss and the expected fair value of the loan is less than its contractual amount. The amount of the impairment may be determined based on the estimated present value of future cash flows, the fair value of the underlying collateral, or the loan s observable market price. Impaired loans with a specifically allocated allowance based on cash flow analysis or the value of the underlying collateral are classified as Level 3 assets, while those with a specifically allocated allowance based on an observable market price that reflects recent sale transactions for similar loans and collateral are classified as Level 2.

The evaluations for impairment are prepared by the responsible relationship managers in our Asset Recovery Group and are reviewed and approved by the Asset Recovery Group Executive. The Asset Recovery Group is part of the Risk Management Group and reports to our Chief Risk Officer. These evaluations are performed in conjunction with the quarterly ALLL process.

Subject loans are evaluated for impairment on a quarterly basis. Loans included in the previous quarter s review are reevaluated and if their values are materially different from the prior quarter evaluation, the underlying information (loan balance and in most cases, collateral value) is compared. Material differences are evaluated for reasonableness, and discussions are held between the relationship managers and their senior managers to understand the difference and determine if any adjustment is necessary. The inputs are developed and substantiated on a quarterly basis, based on current borrower developments, market conditions and collateral values.

The following two internal methods are used to value impaired loans:

Cash flow analysis considers internally developed inputs, such as discount rates, default rates, costs of foreclosure and changes in collateral values.

The fair value of the collateral, which may take the form of real estate or personal property, is based on internal estimates, field observations and assessments provided by third-party appraisers. We perform or reaffirm appraisals of collateral-dependent impaired loans at least annually. Appraisals may occur more frequently if the most recent appraisal does not accurately reflect the current market, the debtor is seriously delinquent or chronically past due, or there has been a material deterioration in the performance of the project or condition of the property. Adjustments to outdated appraisals that result in an appraisal value less than the carrying amount of a collateral-dependent impaired loan are reflected in the ALLL.

Impairment valuations are back-tested each quarter, based on a look-back of actual incurred losses on closed deals previously evaluated for impairment. The overall percent variance of actual net charge-offs on closed deals as compared to the specific allocations on such deals is considered in determining each quarter s specific allocations.

***Loans held for sale***. Through a quarterly analysis of our loan portfolios held for sale, which include both performing and nonperforming loans, we determined that adjustments were necessary to record some of the portfolios at the lower of cost or fair value in accordance with GAAP. There were no loans held for sale portfolios adjusted to fair value at September 30, 2013. Loans held for sale portfolios adjusted to fair value totaled $9 million at December 31, 2012, and $10 million at September 30, 2012.

Current market conditions, including updated collateral values, and reviews of our borrowers financial condition influenced the inputs used in our internal models and other valuation methodologies, resulting in these adjustments. The valuations are prepared by the responsible relationship managers or analysts in our Asset Recovery Group and are reviewed and approved by the Asset Recovery Group Executive. Actual gains or losses realized on the sale of various loans held for sale provide a back-testing mechanism for determining the appropriateness of our valuations of these loans held for sale that are adjusted to fair value.

Valuations of performing commercial mortgage and construction loans held for sale are conducted using internal models that rely on market data from sales or nonbinding bids on similar assets, including credit spreads, treasury rates, interest rate curves and risk profiles, as well as our own assumptions about the exit market for the loans and details about individual loans within the respective portfolios. Therefore, we have classified these loans as Level 3 assets. The inputs related to our assumptions and other internal loan data include changes in real estate values, costs of foreclosure, prepayment rates, default rates and discount rates.

Valuations of nonperforming commercial mortgage and construction loans held for sale are based on current agreements to sell the loans or approved discounted payoffs. If a negotiated value is not available, we use third-party appraisals, adjusted for current market conditions. Since valuations are based on unobservable data, these loans have been classified as Level 3 assets.

***Direct financing leases and operating lease assets held for sale***. Our Key Equipment Finance (KEF) Accounting and Capital Markets groups are responsible for the valuation policies and procedures related to these assets. The Managing Director of the KEF Capital Markets group reports to the President of our Equipment Finance line of business. A weekly report is distributed to both groups that lists all Equipment Finance deals booked in the warehouse portfolio. On a quarterly basis, the KEF Accounting group prepares a detailed held-for-sale roll-forward schedule that is reconciled to the general ledger and the above mentioned weekly report. KEF management uses the held-for-sale roll-forward schedule to determine if an impairment adjustment is necessary in accordance with lower of cost or fair value guidelines.

Valuations of direct financing leases and operating lease assets held for sale are performed using an internal model that relies on market data, such as swap rates and bond ratings, as well as our own assumptions about the exit market for the leases and details about the individual leases in the portfolio. The inputs based on our assumptions include changes in the value of leased items and internal credit ratings. These leases have been classified as Level 3 assets. Leases also may be valued using current nonbinding bids when they are available. These leases are classified as Level 2 assets. In a distressed market where market data is not available, an estimate of the fair value of the leased asset may be used to value the lease, resulting in a Level 3 classification. In an inactive market, the market value of the assets held for sale is determined as the present value of the future cash flows discounted at the current buy rate. KEF Accounting calculates an estimated fair value buy rate based on the credit premium inherent in the relevant bond index and the appropriate swap rate on the measurement date. The amount of the adjustment is calculated as book value minus the present value of future cash flows discounted at the calculated buy rate.

***Goodwill and other intangible assets***. On a quarterly basis, we review impairment indicators to determine whether we need to evaluate the carrying amount of the goodwill and other intangible assets assigned to Key Community Bank and Key Corporate Bank. We also perform an annual impairment test for goodwill. New accounting guidance that permits an entity to first assess qualitative factors to determine whether additional goodwill impairment testing is required became effective for us on January 1, 2012. We did not choose to utilize this qualitative assessment in our annual goodwill impairment testing performed during the fourth quarter of 2012. Fair value of our reporting units is determined using both an income approach (discounted cash flow method) and a market approach (using publicly traded company and recent transactions data), which are weighted equally.

Inputs used include market-available data, such as industry, historical and expected growth rates, and peer valuations, as well as internally driven inputs, such as forecasted earnings and market participant insights. Since this valuation relies on a significant number of unobservable inputs, we have classified goodwill as Level 3. We use a third-party valuation services provider to perform the annual, and if necessary, any interim, Step 1 valuation process, and to perform a Step 2 analysis, if needed, on our reporting units. Annual and any interim valuations prepared by the third-party valuation services provider are reviewed by the appropriate individuals within Key to ensure that the assumptions used in preparing the analysis are appropriate and properly supported. For additional information on the results of recent goodwill impairment testing, see Note 10 ( Goodwill and Other Intangible Assets ) on page on 171 of our 2012 Form 10-K.

The fair value of other intangible assets is calculated using a cash flow approach. While the calculation to test for recoverability uses a number of assumptions that are based on current market conditions, the calculation is based primarily on unobservable assumptions. Accordingly, these assets are classified as Level 3. Our lines of business, with oversight from our Accounting group, are responsible for routinely, at least quarterly, assessing whether impairment indicators are present. All indicators that signal impairment may exist are appropriately considered in this analysis. An impairment loss is only recognized for a held and used long lived asset if the sum of its estimated future undiscounted cash flows used to test for recoverability is less than its carrying value.

Our primary assumptions include attrition rates, alternative costs of funds and rates paid on deposits. For additional information on the results of other intangible assets impairment testing, see Note 10 ( Goodwill and Other Intangible Assets ) on page on 171 of our 2012 Form 10-K.

***Other assets***. OREO and other repossessed properties are valued based on inputs such as appraisals and third-party price opinions, less estimated selling costs. Generally, we classify these assets as Level 3, but OREO and other repossessed properties for which we receive binding purchase agreements are classified as Level 2. Returned lease inventory is valued based on market data for similar assets and is classified as Level 2. Assets that are acquired through, or in lieu of, loan foreclosures are recorded initially as held for sale at fair value less estimated selling costs at the date of foreclosure. After foreclosure, valuations are updated periodically, and current market conditions may require the assets to be marked down further to a new cost basis.

Commercial Real Estate Valuation Process: When a loan is reclassified from loan status to OREO because we took possession of the collateral, the Asset Recovery Group Loan Officer, in consultation with our OREO group, obtains a broker price opinion or a third-party appraisal, which is used to establish the fair value of the underlying collateral. The determined fair value of the underlying collateral less estimated selling costs becomes the carrying value of the OREO asset. In addition to valuations from independent third-party sources, our OREO group also writes down the carrying balance of OREO assets once a bona fide offer is contractually accepted, through execution of a Purchase and Sale Agreement, where the accepted price is lower than the current balance of the particular OREO asset. The fair value of OREO property is re-evaluated every 90 days and the OREO asset is adjusted as necessary.

Consumer Real Estate Valuation Process: The Asset Management team within our Risk Operations group is responsible for valuation policies and procedures in this area. The current vendor partner provides monthly reporting of all broker price opinion evaluations, appraisals and the monthly market plans. Market plans are reviewed monthly, and valuations are reviewed and tested monthly to ensure proper pricing has been established and guidelines are being met. Risk Operations Compliance validates and provides periodic testing of the valuation process. The Asset Management team reviews changes in fair value measurements. Third-party broker price opinions are reviewed every 90 days, and the fair value is written down based on changes to the valuation. External factors are documented and monitored as appropriate.

Mortgage servicing assets are valued based on inputs such as prepayment speeds, earn rates, credit default rates, discount rates and servicing advances. We classify these assets as Level 3. Additional information regarding the valuation of mortgage servicing assets is provided in Note 8 ( Mortgage Servicing Assets ).

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**Quantitative Information about Level 3 Fair Value Measurements**

The range and weighted-average of the significant unobservable inputs used to fair value our material Level 3 recurring and nonrecurring assets at September 30, 2013, December 31, 2012, and September 30, 2012, along with the valuation techniques used, are shown in the following table:

| **September 30, 2013** *dollars in millions* | **Fair Value of Level 3 Assets** | **Valuation Technique** | **Significant Unobservable Input** | **Range (Weighted-Average)** |
|---|---|---|---|---|
| **Recurring** | | | | |
| Other investments principal investments direct: | $ 168 | Individual analysis of the condition of each investment | | |
| Debt instruments | | | EBITDA multiple | 5.80 - 7.20% (6.00%) |
| Equity instruments of private companies | | | EBITDA multiple (where applicable) | 4.70 - 9.60% (6.30%) |
| | | | Revenue multiple (where applicable) | 1.00 - 4.80% (4.10%) |
| **Nonrecurring** | | | | |
| Impaired loans | 26 | Fair value of underlying collateral | Discount | 10.00 - 100.00% (35.00%) |
| Goodwill | 979 | Discounted cash flow and market data | Earnings multiple of peers | 9.70 - 14.20 (11.25) |
| | | | Equity multiple of peers | .95 - 1.17 (1.09) |
| | | | Control premium | N/A (30.00%) |
| | | | Weighted-average cost of capital | N/A (13.00%) |

| **December 31, 2012** *dollars in millions* | **Fair Value of Level 3 Assets** | **Valuation Technique** | **Significant Unobservable Input** | **Range (Weighted-Average)** |
|---|---|---|---|---|
| **Recurring** | | | | |
| Other investments principal investments direct: | $ 181 | Individual analysis of the condition of each investment | | |
| Debt instruments | | | EBITDA multiple | 5.50 - 6.00% (5.90%) |
| Equity instruments of private companies | | | EBITDA multiple (where applicable) | 5.00 - 8.50% (6.10%) |
| | | | Revenue multiple (where applicable) | 0.30 - 5.70% (4.80%) |
| **Nonrecurring** | | | | |
| Impaired loans | 25 | Fair value of underlying collateral | Discount | 0.00 - 100.00% (45.00%) |
| Goodwill | 979 | Discounted cash flow and market data | Earnings multiple of peers | 9.70 - 14.20 (11.25) |
| | | | Equity multiple of peers | .95 - 1.17 (1.09) |
| | | | Control premium | N/A (30.00%) |
| | | | Weighted-average cost of capital | N/A (13.00%) |

| September 30, 2012<br>*dollars in millions* | Fair Value of Level 3 Assets | Valuation Technique | Significant Unobservable Input | Range (Weighted-Average) |
|---|---|---|---|---|
| **Recurring** | | | | |
| Other investments principal investments direct: | $ 202 | Individual analysis of the condition of each investment | | |
| Debt instruments | | | EBITDA multiple | 4.90 - 6.00% (5.90%) |
| Equity instruments of private companies | | | EBITDA multiple (where applicable) | 5.50 - 10.80% (6.10%) |
| | | | Revenue multiple (where applicable) | 0.20 - 4.40% (2.80%) |
| **Nonrecurring** | | | | |
| Impaired loans | 52 | Fair value of underlying collateral | Discount | 0.00 - 100.00% (35.00%) |
| Goodwill | 979 | Discounted cash flow and market data | Earnings multiple of peers | 8.30 - 11.90 (10.01) |
| | | | Equity multiple of peers | 1.21 - 1.32 (1.27) |
| | | | Control premium | N/A (32.00%) |
| | | | Weighted-average cost of capital | N/A (15.00%) |

**Fair Value Disclosures of Financial Instruments**

The levels in the fair value hierarchy ascribed to our financial instruments and the related carrying amounts at September 30, 2013, December 31, 2012, and September 30, 2012 are shown in the following table.

| | September 30, 2013 | | | | | |
|---|---|---|---|---|---|---|
| | | Fair Value | | | | |
| *in millions* | Carrying Amount | Level 1 | Level 2 | Level 3 | Netting Adjustment | Total |
| **ASSETS** | | | | | | |
| Cash and short-term investments [a] | **$ 4,283** | **$ 3,767** | **$ 516** | | | **$ 4,283** |
| Trading account assets [e] | **806** | **6** | **800** | | | **806** |
| Securities available for sale [e] | **12,606** | **24** | **12,582** | | | **12,606** |
| Held-to-maturity securities [b] | **4,835** | | **4,730** | | | **4,730** |
| Other investments [e] | **1,007** | | **394** | **$ 613** | | **1,007** |
| Loans, net of allowance [c] | **52,729** | | | **51,301** | | **51,301** |
| Loans held for sale [e] | **699** | | | **699** | | **699** |
| Mortgage servicing assets [d] | **331** | | | **388** | | **388** |
| Derivative assets [e] | **475** | **60** | **1,261** | **23** | **$ (869)** [f] | **475** |
| **LIABILITIES** | | | | | | |
| Deposits with no stated maturity [a] | **$ 61,399** | | **$ 61,399** | | | **$ 61,399** |
| Time deposits [d] | **7,136** | **605** | **6,632** | | | **7,237** |
| Short-term borrowings [a] | **1,921** | **$ 4** | **1,917** | | | **1,921** |
| Long-term debt [d] | **6,154** | **6,192** | **265** | | | **6,457** |
| Derivative liabilities [e] | **450** | **59** | **948** | **$ 2** | **$ (559)** [f] | **450** |

| | December 31, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | | Fair Value | | | | |
| *in millions* | Carrying Amount | Level 1 | Level 2 | Level 3 | Netting Adjustment | Total |
| **ASSETS** | | | | | | |
| Cash and short-term investments [a] | $ 4,525 | $ 4,254 | $ 271 | | | $ 4,525 |
| Trading account assets [e] | 605 | 2 | 600 | $ 3 | | 605 |
| Securities available for sale [e] | 12,094 | 43 | 12,051 | | | 12,094 |
| Held-to-maturity securities [b] | 3,931 | | 3,992 | | | 3,992 |
| Other investments [e] | 1,064 | | 396 | 668 | | 1,064 |
| Loans, net of allowance [c] | 51,934 | | | 51,046 | | 51,046 |
| Loans held for sale [e] | 599 | | | 599 | | 599 |
| Mortgage servicing assets [d] | 204 | | | 238 | | 238 |
| Derivative assets [e] | 693 | 54 | 1,883 | 26 | $ (1,270) [f] | 693 |
| **LIABILITIES** | | | | | | |
| Deposits with no stated maturity [a] | $ 58,132 | | $ 58,132 | | | $ 58,132 |
| Time deposits [d] | 7,861 | $ 408 | 7,612 | | | 8,020 |
| Short-term borrowings [a] | 1,896 | | 1,896 | | | 1,896 |
| Long-term debt [d] | 6,847 | 2,807 | 4,585 | | | 7,392 |
| Derivative liabilities [e] | 584 | 54 | 1,331 | $ 2 | $ (803) [f] | 584 |

| | | September 30, 2012 | | | | |
|---|---|---|---|---|---|---|
| | | Fair Value | | | | |
| *in millions* | **Carrying Amount** | **Level 1** | **Level 2** | **Level 3** | **Netting Adjustment** | **Total** |
| **ASSETS** | | | | | | |
| Cash and short-term investments [a] | $ 3,182 | $ 2,888 | $ 294 | | | $ 3,182 |
| Trading account assets [e] | 663 | 10 | 596 | $ 57 | | 663 |
| Securities available for sale [e] | 11,962 | 27 | 11,934 | 1 | | 11,962 |
| Held-to-maturity securities [b] | 4,153 | | 4,212 | | | 4,212 |
| Other investments [e] | 1,106 | | 395 | | | |