

CAPITAL ONE FINANCIAL CORP
Form 10-Q
November 03, 2014

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, 2014

OR

•• TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____
Commission File No. 1-13300

CAPITAL ONE FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

54-1719854
(I.R.S. Employer
Identification No.)

1680 Capital One Drive,
McLean, Virginia
(Address of Principal Executive Offices)

22102
(Zip Code)

Registrant's telephone number, including area code: (703) 720-1000
(Former name, former address and former fiscal year, if changed since last report)
(Not applicable)

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

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

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

Large accelerated filer ✓ Accelerated filer ••
Non-accelerated filer •• 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 ✓

As of October 31, 2014, there were 555,970,573 shares of the registrant's Common Stock, par value \$.01 per share, outstanding.

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PART I—FINANCIAL INFORMATION

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”)

This discussion contains forward-looking statements that are based upon management’s current expectations and are subject to significant uncertainties and changes in circumstances. Please review “Forward-Looking Statements” for more information on the forward-looking statements in this Quarterly Report on Form 10-Q (“this Report”). Our actual results may differ materially from those included in these forward-looking statements due to a variety of factors including, but not limited to, those described in “Part II—Item 1A. Risk Factors” in this Report and in “Part I—Item 1A. Risk Factors” in our 2013 Annual Report on Form 10-K (“2013 Form 10-K”). Unless otherwise specified, references to notes to our consolidated financial statements refer to the notes to our unaudited consolidated financial statements as of September 30, 2014 included in this Report.

Management monitors a variety of key indicators to evaluate our business results and financial condition. The following MD&A is intended to provide the reader with an understanding of our results of operations, financial condition and liquidity by focusing on changes from year to year in certain key measures used by management to evaluate performance, such as profitability, growth and credit quality metrics. MD&A is provided as a supplement to, and should be read in conjunction with, our unaudited consolidated financial statements and related notes in this Report and the more detailed information contained in our 2013 Form 10-K.

SUMMARY OF SELECTED FINANCIAL DATA

The following table presents selected consolidated financial data from our results of operations for the third quarter and first nine months of 2014 and 2013, and selected comparative balance sheet data as of September 30, 2014 and December 31, 2013. We also provide selected key metrics we use in evaluating our performance. Certain prior period amounts have been recast to conform to the current period presentation. The comparability of our results of operations between reported periods is impacted by the following transactions completed in 2013:

On November 1, 2013, we completed the acquisition of Beech Street Capital, a privately-held, national originator and servicer of Federal National Mortgage Association (“Fannie Mae”), Federal Home Loan Mortgage Corporation (“Freddie Mac”) and Federal Housing Administration (“FHA”) multifamily commercial real estate loans.

On September 6, 2013, we completed the sale of the Best Buy private label and co-branded credit card portfolio to Citibank, N.A (the “Portfolio Sale”). Pursuant to the agreement we received \$6.4 billion for the net portfolio assets. In 2012, we completed the acquisitions of (i) substantially all of the assets and assumed liabilities of HSBC’s credit card and private-label credit card business in the United States (other than the HSBC Bank USA, National Association consumer credit card program and certain other retained assets and liabilities) (the “2012 U.S. card acquisition”); and (ii) substantially all of the ING Direct business in the United States (“ING Direct”) from ING Groep N.V., ING Bank N.V., ING Direct N.V. and ING Direct Bancorp (the “ING Direct acquisition”).

We use the term “Acquired Loans” to refer to a limited portion of the credit card loans acquired in the 2012 U.S. card acquisition and the substantial majority of consumer and commercial loans acquired in the ING Direct and Chevy Chase Bank, F.S.B. (“CCB”) acquisitions, which were recorded at fair value at acquisition and subsequently accounted for based on expected cash flows to be collected (under the accounting standard formerly known as “Statement of Position 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer,” commonly referred to as “SOP 03-3”). The accounting and classification of these loans may significantly alter some of our reported credit quality metrics. We therefore supplement certain reported credit quality metrics with metrics adjusted to exclude the impact of these Acquired Loans. For additional information, see “MD&A—Credit Risk Profile” and “Note 4—Loans.”

Table of ContentsTable 1: Consolidated Financial Highlights (Unaudited)⁽¹⁾

(Dollars in millions, except per share data and as noted)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2014	2013	Change	2014	2013	Change
Income statement						
Net interest income	\$4,497	\$4,560	(1)%	\$13,162	\$13,683	(4)%
Non-interest income	1,142	1,091	5	3,315	3,157	5
Total net revenue ⁽²⁾	5,639	5,651	—	16,477	16,840	(2)
Provision for credit losses	993	849	17	2,432	2,496	(3)
Non-interest expense:						
Marketing	392	299	31	1,052	946	11
Amortization of intangibles	130	161	(19)	409	505	(19)
Acquisition-related	13	37	(65)	54	133	(59)
Operating expenses	2,450	2,612	(6)	7,381	7,534	(2)
Total non-interest expense	2,985	3,109	(4)	8,896	9,118	(2)
Income from continuing operations before income taxes	1,661	1,693	(2)	5,149	5,226	(1)
Income tax provision	536	575	(7)	1,696	1,747	(3)
Income from continuing operations, net of tax	1,125	1,118	1	3,453	3,479	(1)
Loss from discontinued operations, net of tax	(44)	(13)	238	(24)	(210)	(89)
Net income	1,081	1,105	(2)	3,429	3,269	5
Dividends and undistributed earnings allocated to participating securities	(5)	(5)	—	(14)	(14)	—
Preferred stock dividends	(20)	(13)	54	(46)	(39)	18
Net income available to common shareholders	\$1,056	\$1,087	(3)	\$3,369	\$3,216	5
Common share statistics						
Earnings per common share:						
Basic earnings per common share	\$1.89	\$1.87	1	\$5.95	\$5.53	8
Diluted earnings per common share	1.86	1.84	1	5.86	5.46	7
Weighted average common shares outstanding:						
Basic	559.9	582.3	(4)	566.1	581.4	(3)
Diluted	567.9	591.1	(4)	575.2	589.0	(2)
Dividends per common share	\$0.30	\$0.30	—	\$0.90	\$0.65	38
Average balances						
Loans held for investment ⁽³⁾	\$199,422	\$191,135	4	\$196,068	\$192,547	2
Interest-earning assets	268,890	264,796	2	265,065	267,590	(1)
Total assets	299,523	294,919	2	296,175	298,347	(1)
Interest-bearing deposits	179,928	186,752	(4)	181,587	188,877	(4)
Total deposits	205,199	208,340	(2)	205,783	210,170	(2)
Borrowings	40,314	36,355	11	37,332	38,261	(2)
Common equity	43,489	40,332	8	42,772	40,335	6
Total stockholders' equity	44,827	41,185	9	43,828	41,188	6
Selected performance metrics						
Purchase volume ⁽⁴⁾	\$57,474	\$50,943	13	\$161,266	\$146,829	10

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Total net revenue margin ⁽⁵⁾	8.39	% 8.54	% (15) bps	8.29	% 8.39	% (10) bps
Net interest margin ⁽⁶⁾	6.69	6.89	(20)	6.62	6.82	(20)
Return on average assets	1.50	1.52	(2)	1.55	1.55	—
Return on average tangible assets ⁽⁷⁾	1.58	1.60	(2)	1.64	1.64	—
Return on average common equity ⁽⁸⁾	10.12	10.91	(79)	10.58	11.33	(75)
Return on average tangible common equity ⁽⁹⁾	15.73	17.96	(223)	16.66	18.75	(209)
Equity-to-assets ratio	14.97	13.96	101	14.80	13.81	99
Non-interest expense as a % of average loans held for investment	5.99	6.51	(52)	6.05	6.31	(26)
Efficiency ratio ⁽¹⁰⁾	52.93	55.02	(209)	53.99	54.14	(15)

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Capital One Financial Corporation
(COF)

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(Dollars in millions, except per share data and as noted)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2014	2013	Change	2014	2013	Change
Effective income tax rate from continuing operations	32.3	34.0	(170)	32.9	33.4	(50)
Net charge-offs	\$756	\$917	(18)%	\$2,499	\$2,965	(16)%
Net charge-off rate ⁽¹¹⁾	1.52	% 1.92	% (40) bps	1.70	% 2.05	% (35) bps
Net charge-off rate (excluding Acquired Loans)	1.73	2.29	(56)	1.96	2.48	(52)
			September 30,	December 31,		
(Dollars in millions except per share data as noted)			2014	2013		Change
Balance sheet (period end)						
Loans held for investment ⁽³⁾			\$201,592	\$197,199	2	%
Interest-earning assets			270,001	265,170	2	
Total assets			300,202	296,933	1	
Interest-bearing deposits			178,876	181,880	(2)
Total deposits			204,264	204,523	—	
Borrowings			42,243	40,654	4	
Common equity			42,682	40,779	5	
Total stockholders' equity			44,018	41,632	6	
Credit quality metrics (period end)						
Allowance for loan and lease losses			\$4,212	\$4,315	(2)
Allowance as a % of loans held for investment (“allowance coverage ratio”)			2.09	% 2.19	% (10	) bps
Allowance as a % of loans held for investment (excluding Acquired Loans)			2.37	2.54	(17)
30+ day performing delinquency rate			2.46	2.63	(17)
30+ day performing delinquency rate (excluding Acquired Loans)			2.81	3.08	(27)
30+ day delinquency rate			2.76	2.96	(20)
30+ day delinquency rate (excluding Acquired Loans)			3.14	3.46	(32)
Capital ratios ⁽¹²⁾						
Common equity Tier 1 capital ratio			12.73	% N/A	**	
Tier 1 common ratio			N/A	12.19	% **	
Tier 1 risk-based capital ratio			13.31	12.57	74	bps
Total risk-based capital ratio			15.24	14.69	55	
Tier 1 leverage ratio			10.64	10.06	58	
Tangible common equity (“TCE”) ratio ⁽³⁾			9.56	8.89	67	
Associates						
Employees (in thousands), period end ⁽¹⁴⁾			44.9	45.4	(1) %

** Change is not meaningful.

We adopted ASU 2014-01 “Accounting for Investments in Qualified Affordable Housing Projects” (Investments in Qualified Affordable Housing Projects) as of January 1, 2014. See “Note 1—Summary of Significant Accounting Policies” for additional information. Prior period results and related metrics have been recast to conform to this presentation.

(2) Total net revenue was reduced by \$164 million and \$480 million in the third quarter and first nine months of 2014, respectively, and by \$154 million and \$611 million in the third quarter and first nine months of 2013, respectively,

for the estimated uncollectible amount of billed finance charges and fees.

- (3) Loans held for investment includes loans acquired in the CCB, ING Direct and 2012 U.S. card acquisitions. See “Note 4—Loans” for additional information on Acquired Loans.
- (4) Consists of credit card purchase transactions, net of returns, for the period for both loans classified as held for investment and loans classified as held for sale. Excludes cash advance and balance transfer transactions.
- (5) Calculated based on annualized total net revenue for the period divided by average interest-earning assets for the period.
- (6) Calculated based on annualized net interest income for the period divided by average interest-earning assets for the period.
Calculated based on annualized income from continuing operations, net of tax, for the period divided by average tangible assets for the period. See “MD&A—Supplemental Tables—Table A: Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures” for additional information.
- (7) Calculated based on the annualized sum of (i) income from continuing operations, net of tax; (ii) less dividends and undistributed earnings allocated to participating securities; (iii) less preferred stock dividends, for the period, divided by average common equity. Our calculation of return on average common equity may not be comparable to similarly titled measures reported by other companies.
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- Calculated based on the annualized sum of (i) income from continuing operations, net of tax; (ii) less dividends and undistributed earnings allocated to participating securities; (iii) less preferred stock dividends, for the period,
- (9) divided by average tangible common equity. Our calculation of return on average tangible common equity may not be comparable to similarly titled measures reported by other companies. See “MD&A—Supplemental Tables—Table A: Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures” for additional information.
- (10) Calculated based on non-interest expense for the period divided by total net revenue for the period.
- (11) Calculated based on annualized net charge-offs for the period divided by average loans held for investment for the period.
- Beginning on January 1, 2014, we calculate our regulatory capital under Basel III Standardized Approach subject to transition provisions. Prior to the first quarter of 2014, we calculated regulatory capital measures under Basel I.
- (12) See “MD&A—Capital Management” and “MD&A—Supplemental Tables—Table A: Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures” for additional information, including the calculation of each of these ratios.
- TCE ratio is a non-GAAP measure calculated based on tangible common equity divided by tangible assets. See
- (13) “MD&A—Supplemental Tables—Table A: Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures” for the calculation of this measure and reconciliation to the comparative GAAP measure.
- In the second quarter of 2014, we changed our presentation from total full-time equivalent employees to total employees. All prior periods have been recast to conform to the current presentation. During this change, we
- (14) determined that we had previously understated the total number of full-time equivalent employees by approximately 7%.

INTRODUCTION

General

We are a diversified financial services holding company with banking and non-banking subsidiaries. Capital One Financial Corporation and its subsidiaries (the “Company”) offer a broad array of financial products and services to consumers, small businesses and commercial clients through branches, the internet and other distribution channels. As of September 30, 2014, our principal subsidiaries included:

Capital One Bank (USA), National Association (“COBNA”), which offers credit and debit card products, other lending products and deposit products; and

Capital One, National Association (“CONA”), which offers a broad spectrum of banking products and financial services to consumers, small businesses and commercial clients.

The Company is hereafter collectively referred to as “we,” “us” or “our.” COBNA and CONA are collectively referred to as the “Banks.” Certain business terms used in this document are defined in the “Glossary and Acronyms” section and should be read in conjunction with the consolidated financial statements included in this Report.

We had total loans held for investment of \$201.6 billion, deposits of \$204.3 billion and stockholders’ equity of \$44.0 billion as of September 30, 2014, compared with total loans held for investment of \$197.2 billion, deposits of \$204.5 billion and stockholders’ equity of \$41.6 billion as of December 31, 2013.

Our consolidated total net revenues are derived primarily from lending to consumer and commercial customers net of funding costs associated with interest on deposits, short-term borrowings and long-term debt. We also earn non-interest income which primarily consists of interchange income net of reward expenses and service charges and other customer-related fees. Our expenses primarily consist of the provision for credit losses, operating expenses (including salaries and associate benefits, occupancy and equipment costs, professional services, communication and data processing expenses and other miscellaneous expenses), marketing expenses and income taxes.

Our principal operations are currently organized for management reporting purposes into three primary business segments, which are defined primarily based on the products and services provided or the type of customer served: Credit Card, Consumer Banking and Commercial Banking. The operations of acquired businesses have been integrated into our existing business segments. Certain activities that are not part of a segment, such as management of our corporate investment portfolio and asset/liability management by our centralized Corporate Treasury group, are

included in the Other category.

Credit Card: Consists of our domestic consumer and small business card lending, national closed-end installment lending and the international card lending businesses in Canada and the United Kingdom.

Consumer Banking: Consists of our branch-based lending and deposit gathering activities for consumers and small businesses, national deposit gathering, national auto lending and consumer home loans lending and servicing activities.

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Commercial Banking: Consists of our lending, deposit gathering and servicing activities provided to commercial real estate and commercial and industrial customers. Our commercial and industrial customers typically include companies with annual revenues between \$10 million and \$1 billion.

Table 2 summarizes our business segment results, which we report based on income from continuing operations, net of tax, for the third quarter and first nine months of 2014 and 2013. We provide information on the allocation methodologies used to derive our business segment results in “Note 19—Business Segments” in our 2013 Form 10-K. We also provide a reconciliation of our total business segment results to our results based on the accounting principles generally accepted in the U.S. (“U.S. GAAP”) results in “Note 13—Business Segments” of this Report.

Table 2: Business Segment Results⁽¹⁾

(Dollars in millions)	Three Months Ended September 30,						2013					
	2014		Net Income ⁽³⁾		Total Net Revenue ⁽²⁾		2013		Total Net Revenue ⁽²⁾		Net Income (Loss) ⁽³⁾	
	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
Credit Card	\$3,473	62 %	\$624	55 %	\$3,591	64 %	\$694	62 %				
Consumer Banking	1,604	28	289	26	1,665	29	345	31				
Commercial Banking ⁽⁴⁾	561	10	182	16	511	9	162	14				
Other ⁽⁵⁾	1	—	30	3	(116)	(2)	(83)	(7)				
Total from continuing operations	\$5,639	100 %	\$1,125	100 %	\$5,651	100 %	\$1,118	100 %				
(Dollars in millions)	Nine Months Ended September 30,						2013					
	2014		Net Income ⁽³⁾		Total Net Revenue ⁽²⁾		2013		Total Net Revenue ⁽²⁾		Net Income (Loss) ⁽³⁾	
	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
Credit Card	\$10,083	61 %	\$1,960	57 %	\$10,878	64 %	\$2,099	60 %				
Consumer Banking	4,788	29	953	28	4,991	30	1,172	34				
Commercial Banking ⁽⁴⁾	1,614	10	490	14	1,491	9	536	15				
Other ⁽⁵⁾	(8)	—	50	1	(520)	(3)	(328)	(9)				
Total from continuing operations	\$16,477	100 %	\$3,453	100 %	\$16,840	100 %	\$3,479	100 %				

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in

(1) Qualified Affordable Housing Projects. See “Note 1—Summary of Significant Accounting Policies” for additional information. Prior periods have been recast to conform to this presentation.

(2) Total net revenue consists of net interest income and non-interest income.

(3) Net income for our business segments is reported based on income from continuing operations, net of tax.

(4) On investments that generate tax-exempt income or tax credits, we make certain reclassifications to our Commercial Banking business results to present revenues on a taxable-equivalent basis.

(5) Includes the residual impact of the allocation of certain items, our centralized Corporate Treasury group activities, as well as other items as described in “Note 19—Business Segments” in our 2013 Form 10-K.

EXECUTIVE SUMMARY AND BUSINESS OUTLOOK

We reported net income of \$1.1 billion (\$1.86 per diluted common share) on total net revenue of \$5.6 billion and net income of \$3.4 billion (\$5.86 per diluted common share) on total net revenue of \$16.5 billion for the third quarter and first nine months of 2014, respectively. In comparison, we reported net income of \$1.1 billion (\$1.84 per diluted common share) on total net revenue of \$5.7 billion and net income of \$3.3 billion (\$5.46 per diluted common share) on total net revenue of \$16.8 billion for the third quarter and first nine months of 2013, respectively.

Beginning on January 1, 2014, we calculate our regulatory capital under the Basel III Standardized Approach subject to transition provisions. Our common equity Tier 1 capital ratio, as calculated under the Basel III Standardized Approach, including transition

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provisions, was 12.73% as of September 30, 2014. Our Tier 1 common ratio, as calculated under Basel I, was 12.19% as of December 31, 2013. These numbers are not directly comparable due to methodological differences in the calculation of the ratios.

On March 26, 2014, we announced that our Board of Directors had authorized the repurchase of up to \$2.5 billion of shares of our common stock (“2014 Stock Repurchase Program”). During the second and third quarters of 2014, we have repurchased approximately \$1.5 billion of common stock and expect to complete the 2014 Stock Repurchase Program by the end of the first quarter of 2015. See “Capital Management” below for additional information.

Below are additional highlights of our performance in the third quarter and first nine months of 2014. These highlights generally are based on a comparison between the results of the third quarter and first nine months of 2014 and 2013, except as otherwise noted. The changes in our financial condition and credit performance are generally based on our financial condition and credit performance as of September 30, 2014, compared to December 31, 2013. We provide a more detailed discussion of our financial performance in the sections following this “Executive Summary and Business Outlook.”

Total Company

Earnings: Our net income decreased by \$24 million in the third quarter of 2014, or 2%, to \$1.1 billion, and our net income increased by \$160 million in the first nine months of 2014, or 5%, to \$3.4 billion, compared to \$3.3 billion for the first nine months of 2013. The increase in net income for the first nine months of 2014 was driven by (i) a net provision of \$19 million for mortgage representation and warranty losses (which includes a benefit of \$15 million before taxes in continuing operations and a provision of \$34 million before taxes in discontinued operations) for the first nine months of 2014, compared to a net provision of \$276 million (which includes a benefit of \$27 million before taxes in continuing operations and a provision of \$303 million before taxes in discontinued operations) for the first nine months of 2013; (ii) lower non-interest expenses due to lower amortization of intangibles, acquisition-related costs and the provision for litigation matters; (iii) a decrease in interest expense due to lower funding costs; and (iv) a decrease in provision for credit losses driven by a lower net charge-offs partially offset by a lower release in the allowance for loan and lease losses. These items were partially offset by a decrease in net interest income attributable to lower average interest-earning assets partly due to the Portfolio Sale.

Loans Held for Investment: Period-end loans held for investment increased by \$4.4 billion, or 2%, in the first nine months of 2014, to \$201.6 billion as of September 30, 2014, from \$197.2 billion as of December 31, 2013. The increase was due to commercial and industrial and commercial and multifamily real estate loan growth in our Commercial Banking business, and continued strong auto loan originations outpacing the run-off of the acquired home loan portfolio in our Consumer Banking business. Overall, there was a decline in our credit card loan portfolio primarily due to seasonality, partially offset by loan growth in the second and third quarters of 2014.

Net Charge-off and Delinquency Statistics: Our net charge-off rate decreased by 40 basis points to 1.52% in the third quarter of 2014, compared to 1.92% in the third quarter of 2013, and our net charge-off rate decreased by 35 basis points in the first nine months of 2014, to 1.70%, compared to 2.05% for the first nine months of 2013. The extremely low net charge-off rate in the third quarter 2014, based on our historical trends, was largely due to continued economic improvement and portfolio seasoning. Our reported 30+ day delinquency rate declined to 2.76% as of September 30, 2014, from 2.96% as of December 31, 2013, and 2.88% as of September 30, 2013. The decrease from December 31, 2013 was primarily due to seasonality and strong credit performance. We provide additional information on our credit quality metrics below under “Business Segment Financial Performance” and “Credit Risk Profile.”

Allowance for Loan and Lease Losses: Our allowance for loan and lease losses decreased by \$103 million from \$4.3 billion as of December 31, 2013 and increased by \$214 million, from \$4.0 billion as of June 30, 2014, to \$4.2 billion as of September 30, 2014. The allowance coverage ratio declined to 2.09% as of September 30, 2014, from 2.19% as of December 31, 2013. The release in allowance for loan and lease losses in the first and second quarters of 2014 was mainly due to credit improvements, partially offset by a build in the third quarter of 2014 driven by loan growth and higher delinquency inventories increasing our loss expectations.

Representation and Warranty Reserve: The mortgage representation and warranty reserve decreased by \$92 million to \$1.1 billion as of September 30, 2014, from \$1.2 billion as of December 31, 2013. We recorded a net provision for mortgage representation and warranty losses of \$19 million (which includes a benefit of \$15 million before taxes in continuing operations and provision of \$34 million before taxes in discontinued operations) in the first nine months of 2014. The decrease in representation and warranty reserve was primarily driven by claims paid and legal developments.

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Business Segment Financial Performance

Credit Card: Our Credit Card business generated net income from continuing operations of \$624 million and \$2.0 billion in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$694 million and \$2.1 billion in the third quarter and first nine months of 2013, respectively. The decreases in net income for the third quarter of 2014 compared to the third quarter of 2013, was due to lower net revenue driven by the Portfolio Sale in the third quarter of 2013 and higher provision for credit losses due to a build in the allowance for loan and lease losses driven by loan growth partially offset by lower net charge-offs. These drivers were partially offset by a lower provision for litigation matters and operating efficiencies. The decrease in net income for the first nine months of 2014 compared to the first nine months of 2013 was driven by lower net revenue associated with the Portfolio Sale in the third quarter of 2013, partially offset by a lower provision for credit losses driven by lower net charge-offs and lower non-interest expenses. Period-end loans held for investment in our Credit Card business decreased by \$674 million to \$80.6 billion as of September 30, 2014 from \$81.3 billion as of December 31, 2013. The decrease was largely due to seasonality, partially offset by growth in the domestic card loan portfolio in the second and third quarters of 2014.

Consumer Banking: Our Consumer Banking business generated net income from continuing operations of \$289 million and \$953 million in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$345 million and \$1.2 billion in the third quarter and first nine months of 2013, respectively. The decrease in net income for these periods was primarily attributable to compression in deposit spreads in retail banking, partially offset by higher net interest income generated by growth in our auto loans. Period-end loans held for investment in our Consumer Banking business increased by \$299 million to \$71.1 billion as of September 30, 2014, from \$70.8 billion as of December 31, 2013, due to growth in our auto loan portfolio outpacing the run-off in our acquired home loan portfolio.

Commercial Banking: Our Commercial Banking business generated net income from continuing operations of \$182 million and \$490 million in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$162 million and \$536 million in the third quarter and first nine months of 2013, respectively. The increase in net income for the third quarter 2014 compared to the third quarter 2013 was primarily driven by higher net revenue related to growth in our commercial loan portfolio, partially offset by increases in operating expenses associated with continued investments in business growth and the Beech Street Capital acquisition. The decrease in net income for the first nine months of 2014 compared to the first nine months of 2013 was primarily due to a higher provision for credit losses, reflecting an allowance build in the first nine months of 2014 compared to an allowance release in the first nine months of 2013. Period-end loans held for investment in our Commercial Banking business increased by \$4.8 billion to \$49.8 billion as of September 30, 2014, from \$45.0 billion as of December 31, 2013. The increase was driven by strong loan originations in the commercial and industrial and commercial and multifamily real estate businesses.

Business Outlook

We discuss below our current expectations regarding our total company performance and the performance of each of our business segments over the near-term based on market conditions, the regulatory environment and our business strategies as of the time we filed this Report. The statements contained in this section are based on our current expectations regarding our outlook for our financial results and business strategies. Our expectations take into account, and should be read in conjunction with, our expectations regarding economic trends and analysis of our business as discussed in “Part I—Item 1. Business” and “Part I—Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our 2013 Form 10-K. Certain statements are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Actual results could differ materially from those in our forward-looking statements. Except as otherwise disclosed, forward-looking statements do not reflect: (i) any change in current dividend or repurchase strategies; (ii) the effect of any acquisitions, divestitures or similar transactions that have not been previously disclosed; or (iii) any changes in laws, regulations or regulatory interpretations, in each case after the date as of which such statements are made. See “Forward-Looking Statements” in

this Report for more information on forward-looking statements included in this Report and “Item 1A. Risk Factors” in our 2013 Form 10-K for factors that could materially influence our results.

Total Company Expectations

We continue to expect 2014 pre-provision earnings, excluding non-recurring items, of approximately \$10 billion. On a quarterly basis, we expect both operating expenses and marketing to increase in the fourth quarter of 2014. On an annual basis, we expect operating expenses and marketing to be higher in 2015 than 2014. Both the quarterly and annual expectations are driven by loan

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growth, as well as investments to drive future growth, be a digital leader and keep pace with rising industry regulatory requirements. We expect that future card growth will likely drive allowance builds in coming quarters.

We expect growth in full-year revenues in 2015, driven by strong growth in average loans. While the efficiency ratio will vary from quarter to quarter, we expect the full-year 2015 efficiency ratio to be between 53% and 54%, excluding non-recurring items.

The Federal Reserve did not object to our capital plan submitted in the 2014 CCAR cycle. Pursuant to the capital plan, we expect to maintain our quarterly dividend of \$0.30 per share, subject to approval by the Board of Directors. In addition, the Board of Directors authorized the establishment of a share repurchase program to repurchase up to \$2.5 billion of shares of our common stock through the end of the first quarter of 2015. Under this program, we repurchased approximately \$1.5 billion of our shares in the second and third quarters of 2014, and we expect to repurchase an additional \$1.0 billion over the next two quarters.

The timing and exact amount of any common stock repurchases will depend on various factors, including market conditions, our capital position and amount of our retained earnings. Our 2014 Stock Repurchase Program does not include specific price targets, may be executed through open market purchases or privately negotiated transactions, including utilizing Rule 10b5-1 programs, and may be suspended at any time. See “MD&A—Capital Management—Capital Planning and Regulatory Stress Testing” for more information.

Business Segment Expectations

Credit Card: In our Domestic Card business, we expect increases in the net charge-off rate in the fourth quarter of 2014 and first quarter of 2015 primarily driven by seasonality. Longer term, we expect loan growth to impact the Domestic Card net charge-off rate in 2015. While this impact on the net charge-off rate will be modest at first, we expect it to grow throughout 2015. Overall, we expect the quarterly Domestic Card net charge-off rate throughout 2015 to be in the mid-to-high three percent range. We also expect allowance additions resulting primarily from future loan growth. We believe that our Domestic Card business continues to be well-positioned and will continue to deliver strong and resilient returns.

Consumer Banking: In our Consumer Banking business, we expect auto returns will continue to decline, but remain within ranges that support an attractive business. In addition, we expect the impact of the prolonged low interest rate environment to continue to pressure the returns of our retail banking business, even if rates rise in 2015.

Commercial Banking: In our Commercial Banking business, competition continues to increase, pressuring margins and returns. As competition continues to increase, we expect the pace of the growth in our Commercial Banking business will be slower in 2015 and closer to overall industry growth rates. We continue to expect our focused and specialized approach to deliver strong results in 2015.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with U.S. GAAP requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expenses in the consolidated financial statements. Understanding our accounting policies and the extent to which we use management judgment and estimates in applying these policies is integral to understanding our financial statements. We provide a summary of our significant accounting policies under “Note 1—Summary of Significant Accounting Policies” in our 2013 Form 10-K.

We have identified the following accounting policies as critical because they require significant judgments and assumptions about highly complex and inherently uncertain matters and the use of reasonably different estimates and assumptions could have a material impact on our reported results of operations or financial condition. These critical accounting policies govern:

- Loan loss reserves
- Asset impairment
- Fair value of financial instruments
- Representation and warranty reserves
 - Customer rewards reserves

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We evaluate our critical accounting estimates and judgments on an ongoing basis and update them, as necessary, based on changing conditions. Management has discussed each of these critical accounting policies, related estimates and judgments with the Audit Committee of the Board of Directors.

We provide additional information on our critical accounting policies and estimates under “MD&A—Critical Accounting Policies and Estimates” in our 2013 Form 10-K.

ACCOUNTING CHANGES AND DEVELOPMENTS

Accounting for Investments in Qualified Affordable Housing Projects

In January 2014, the Financial Accounting Standards Board (“FASB”) issued guidance permitting an entity to account for Investments in Qualified Affordable Housing Projects using the proportional amortization method, if certain criteria are met. The proportional method amortizes the cost of the investment over the period in which the investor expects to receive tax credits and other tax benefits, and the resulting amortization is recognized as a component of income taxes attributable to continuing operations. Historically, these investments were under the equity method of accounting and the passive losses related to the investments were recognized within non-interest expense. Prior period results and related metrics have been recast. See “Note 1—Summary of Significant Accounting Policies” for more information.

CONSOLIDATED RESULTS OF OPERATIONS

The section below provides a comparative discussion of our consolidated financial performance for the third quarter and first nine months of 2014 and 2013. Following this section, we provide a discussion of our business segment results. You should read this section together with our “Executive Summary and Business Outlook,” where we discuss trends and other factors that we expect will affect our future results of operations.

Net Interest Income

Net interest income represents the difference between the interest income, including certain fees, earned on our interest-earning assets and the interest expense on our interest-bearing liabilities. Interest-earning assets include loans, investment securities and other interest-earning assets and interest-bearing liabilities include interest-bearing deposits, securitized debt obligations, senior and subordinated notes, and other borrowings. Generally, we include in interest income any past due fees on loans that we deem collectible. Our net interest margin, based on our consolidated results, represents the difference between the yield on our interest-earning assets and the cost of our interest-bearing liabilities, including the notional impact of non-interest bearing funding. We expect net interest income and our net interest margin to fluctuate based on changes in interest rates and changes in the amount and composition of our interest-earning assets and interest-bearing liabilities.

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Table 3 below presents, for each major category of our interest-earning assets and interest-bearing liabilities, the average outstanding balances, interest income earned, interest expense incurred, average yield and rate for the third quarter and first nine months of 2014 and 2013.

Table 3: Average Balances, Net Interest Income and Net Interest Yield⁽¹⁾

(Dollars in millions)	Three Months Ended September 30, 2014			2013		
	Average Balance	Interest Income/ Expense ⁽²⁾⁽³⁾	Yield/ Rate	Average Balance	Interest Income/ Expense ⁽²⁾⁽³⁾	Yield/ Rate
Assets:						
Interest-earning assets:						
Loans:						
Credit card:						
Domestic credit card	\$71,776	\$ 2,594	14.46 %	\$74,421	\$ 2,738	14.72 %
International credit card	7,710	317	16.45	7,782	318	16.35
Total credit card	79,486	2,911	14.65	82,203	3,056	14.87
Consumer banking	71,237	1,100	6.18	71,886	1,112	6.19
Commercial banking	49,218	417	3.39	41,584	402	3.87
Other	125	35	112.00	166	9	21.69
Total loans, including loans held for sale	200,066	4,463	8.92	195,839	4,579	9.35
Investment securities	62,582	398	2.54	63,317	396	2.50
Cash equivalents and other interest-earning assets	6,242	26	1.67	5,640	23	1.63
Total interest-earning assets	\$268,890	\$ 4,887	7.27	\$264,796	\$ 4,998	7.55
Cash and due from banks	2,907			2,553		
Allowance for loan and lease losses	(3,995)			(4,408)		
Premises and equipment, net	3,778			3,784		
Other assets	27,943			28,194		
Total assets	\$299,523			\$294,919		
Liabilities and stockholders' equity:						
Interest-bearing liabilities:						
Deposits	\$179,928	\$ 271	0.60	\$186,752	\$ 309	0.66
Securitized debt obligations	10,110	32	1.27	10,243	42	1.64
Senior and subordinated notes	17,267	71	1.64	12,314	76	2.47
Other borrowings	12,937	16	0.49	13,798	11	0.32
Total interest-bearing liabilities	\$220,242	\$ 390	0.71	\$223,107	\$ 438	0.79
Non-interest bearing deposits	25,271			21,588		
Other liabilities	9,183			9,039		
Total liabilities	254,696			253,734		
Stockholders' equity	44,827			41,185		
Total liabilities and stockholders' equity	\$299,523			\$294,919		
Net interest income/spread		\$ 4,497	6.56		\$ 4,560	6.76
Impact of non-interest bearing funding			0.13			0.13
Net interest margin			6.69 %			6.89 %

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(Dollars in millions)	Nine Months Ended September 30, 2014			2013		
	Average Balance	Interest Income/ Expense ⁽²⁾⁽³⁾	Yield/ Rate	Average Balance	Interest Income/ Expense ⁽²⁾⁽³⁾	Yield/ Rate
Assets:						
Interest-earning assets:						
Loans:						
Credit card:						
Domestic credit card	\$70,321	\$ 7,491	14.20 %	\$76,493	\$ 8,336	14.53 %
International credit card	7,674	954	16.58	7,998	970	16.17
Total credit card	77,995	8,445	14.44	84,491	9,306	14.69
Consumer banking	71,042	3,297	6.19	73,127	3,309	6.03
Commercial banking	47,324	1,224	3.45	39,909	1,158	3.87
Other	131	83	84.48	174	51	39.08
Total loans, including loans held for sale	196,492	13,049	8.85	197,701	13,824	9.32
Investment securities	62,411	1,223	2.61	63,725	1,161	2.43
Cash equivalents and other interest-earning assets	6,162	80	1.73	6,164	74	1.60
Total interest-earning assets	\$265,065	\$ 14,352	7.22	\$267,590	\$ 15,059	7.50
Cash and due from banks	2,853			2,401		
Allowance for loan and lease losses	(4,132)			(4,653)		
Premises and equipment, net	3,808			3,750		
Other assets	28,581			29,259		
Total assets	\$296,175			\$298,347		
Liabilities and stockholders' equity:						
Interest-bearing liabilities:						
Deposits	\$181,587	\$ 819	0.60	\$188,877	\$ 953	0.67
Securitized debt obligations	10,419	109	1.39	10,975	143	1.74
Senior and subordinated notes	15,822	226	1.90	12,331	240	2.60
Other borrowings	11,091	36	0.43	14,955	40	0.36
Total interest-bearing liabilities	\$218,919	\$ 1,190	0.72	\$227,138	\$ 1,376	0.81
Non-interest bearing deposits	24,196			21,293		
Other liabilities	9,232			8,728		
Total liabilities	252,347			257,159		
Stockholders' equity	43,828			41,188		
Total liabilities and stockholders' equity	\$296,175			\$298,347		
Net interest income/spread		\$ 13,162	6.50		\$ 13,683	6.69
Impact of non-interest bearing funding			0.12			0.13
Net interest margin			6.62 %			6.82 %

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in
⁽¹⁾ Qualified Affordable Housing Projects. See "Note 1—Summary of Significant Accounting Policies" for additional
information. Prior periods have been recast to conform to this presentation.

Past due fees included in interest income totaled approximately \$368 million and \$1.1 billion in the third quarter
⁽²⁾ and first nine months of 2014, respectively, and \$440 million and \$1.4 billion in the third quarter and first nine
months of 2013, respectively.

⁽³⁾

Interest income and interest expense and the calculation of average yields on interest-earning assets and average rates on interest-bearing liabilities include the impact of hedge accounting.

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Net interest income decreased by \$63 million, or 1%, from the third quarter of 2013 to \$4.5 billion in the third quarter of 2014. Net interest income decreased by \$521 million, or 4% from the first nine months of 2013 to \$13.2 billion in the first nine months of 2014. These decreases were primarily driven by the Portfolio Sale in 2013, partially offset by growth in lower yielding commercial and auto loans, lower fundings costs and higher yielding investment securities. Average Interest-Earning Assets: The increase in average interest-earning assets in the third quarter of 2014, compared to the third quarter of 2013 was due to continued strong growth in commercial, auto and credit card loans, partially offset by the run-off in our acquired home loan portfolio within our Consumer Banking business and the Portfolio Sale in the third quarter of 2013. The decrease in average interest-earning assets in the first nine months of 2014, compared to the first nine months of 2013, was primarily driven by the Portfolio Sale in the third quarter of 2013, the run-off in our acquired home loan portfolio within our Consumer Banking business, partially offset by continued strong growth in commercial, auto and credit card loans. The decrease in average investment securities was due to sales and paydowns outpacing purchases.

Net Interest Margin: The decrease in our net interest margin in the third quarter of 2014, compared to the third quarter of 2013, and in the first nine months of 2014, compared to the first nine months of 2013, was primarily due to lower average loan yields driven by the Portfolio Sale in 2013 and a shift in the mix of the loan portfolio to lower yielding commercial and auto loans, partially offset by a reduction in our cost of funds and higher yielding investment securities.

Table 4 displays the change in our net interest income between periods and the extent to which the variance is attributable to: (i) changes in the volume of our interest-earning assets and interest-bearing liabilities; or (ii) changes in the interest rates related to these assets and liabilities.

Table 4: Rate/Volume Analysis of Net Interest Income⁽¹⁾

(Dollars in millions)	Three Months Ended September 30, 2014 vs 2013			Nine Months Ended September 30, 2014 vs. 2013		
	Total Variance	Volume	Rate	Total Variance	Volume	Rate
Interest income:						
Loans:						
Credit card	\$(145)	\$(100)	\$(45)	\$(861)	\$(706)	\$(155)
Consumer banking	(12)	(10)	(2)	(12)	(94)	82
Commercial banking	15	65	(50)	66	192	(126)
Other	26	(2)	28	32	(13)	45
Total loans, including loans held for sale	(116)	(47)	(69)	(775)	(621)	(154)
Investment securities	2	(5)	7	62	(24)	86
Cash equivalents and other interest-earning assets	3	2	1	6	—	6
Total interest income	(111)	(50)	(61)	(707)	(645)	(62)
Interest expense:						
Deposits	(38)	(11)	(27)	(134)	(36)	(98)
Securitized debt obligations	(10)	—	(10)	(34)	(7)	(27)
Senior and subordinated notes	(5)	20	(25)	(14)	50	(64)
Other borrowings	5	(1)	6	(4)	(10)	6
Total interest expense	(48)	8	(56)	(186)	(3)	(183)
Net interest income	\$(63)	\$(58)	\$(5)	\$(521)	\$(642)	\$121

⁽¹⁾ We calculate the change in interest income and interest expense separately for each item. The portion of interest income or interest expense attributable to both volume and rate is allocated proportionately when the calculation results in a positive value. When the portion of interest income or interest expense attributable to both volume and rate results in a negative value, the total amount is allocated to volume or rate, depending on which amount is

positive.

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Capital One Financial Corporation
(COF)

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Non-Interest Income

Non-interest income primarily consists of interchange income net of rewards expense, service charges and other customer-related fees and other non-interest income. Other non-interest income includes the pre-tax net provision (benefit) for mortgage representation and warranty losses related to continuing operations. It also includes gains and losses from the sale of investment securities, gains and losses on derivatives not accounted for in hedge accounting relationships, as well as hedge ineffectiveness.

Table 5 displays the components of non-interest income for the third quarter and first nine months of 2014 and 2013.

Table 5: Non-Interest Income

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
(Dollars in millions)				
Service charges and other customer-related fees	\$471	\$530	\$1,405	\$1,614
Interchange fees, net	523	476	1,498	1,407
Net other-than-temporary impairment	(9)	(11)	(15)	(40)
Other non-interest income:				
Benefit for mortgage representation and warranty losses ⁽¹⁾	—	13	15	27
Net gains from the sale of investment securities	6	—	18	3
Net fair value gains (losses) on free-standing derivatives	11	(8)	37	(11)
Other	140	91	357	157
Total other non-interest income	157	96	427	176
Total non-interest income	\$1,142	\$1,091	\$3,315	\$3,157

⁽¹⁾ Represents the benefit for mortgage representation and warranty losses recorded in continuing operations. For the total impact to the net provision for mortgage representation and warranty losses, including the portion recognized on our consolidated statements of income as a component of discontinued operations, see “MD&A—Consolidated Balance Sheets Analysis—Table 14: Changes in Representation and Warranty Reserve.”

Non-interest income increased by \$51 million, or 5%, to \$1.1 billion in the third quarter of 2014, and by \$158 million, or 5%, to \$3.3 billion in the first nine months of 2014, from \$3.2 billion in the first nine months of 2013. The main driver for the increases in non-interest income was an increase in interchange fees, net, due to strong purchase volume in our credit card loan portfolio, partially offset by a decline in our service charges and other customer-related fees.

Provision for Credit Losses

Our provision for credit losses in each period is driven by net charge-offs, changes to the allowance for loan and lease losses and changes to the reserve for unfunded lending commitments. We recorded a provision for credit losses of \$993 million and \$2.4 billion in the third quarter and first nine months of 2014, respectively, compared with \$849 million and \$2.5 billion in the third quarter and first nine months of 2013, respectively.

The increase in the provision for credit losses of \$144 million in the third quarter of 2014 compared to the third quarter of 2013 was primarily driven by an increase in the allowance for loan and lease losses due to higher loan volumes and higher delinquencies in the domestic card loan portfolio, partially offset by lower net charge-offs.

The decrease in the provision for credit losses of \$64 million in the first nine months of 2014 compared to the first nine months of 2013, due to lower net charge-offs driven by improved credit, partially offset by a smaller release of our allowance for loan and lease losses.

We provide additional information on the provision for credit losses and changes in the allowance for loan and lease losses within “Credit Risk Profile—Summary of Allowance for Loan and Lease Losses,” “Note 4—Loans” and “Note 5—Allowance for Loan and Lease Losses.” For information on the allowance methodology for each of our loan categories, see “Note 1—Summary of Significant Accounting Policies” in our 2013 Form 10-K.

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Non-Interest Expense

Non-interest expense consists of ongoing operating costs, such as salaries and associate benefits, occupancy and equipment costs, professional services, communications and data processing expenses and other miscellaneous expenses, as well as marketing costs, acquisition-related expenses and amortization of intangibles.

Table 6 displays the components of non-interest expense for the third quarter and first nine months of 2014 and 2013.

Table 6: Non-Interest Expense⁽¹⁾⁽²⁾

	Three Months		Nine Months Ended	
	Ended September 30,		September 30,	
(Dollars in millions)	2014	2013	2014	2013
Salaries and associate benefits	\$1,128	\$1,152	\$3,414	\$3,365
Occupancy and equipment	419	376	1,271	1,104
Marketing	392	299	1,052	946
Professional services	304	328	887	990
Communications and data processing	196	225	595	677
Amortization of intangibles	130	161	409	505
Other non-interest expense:				
Collections	90	114	287	362
Fraud losses	67	56	197	161
Bankcard, regulatory and other fee assessments	118	151	345	431
Other	141	247	439	577
Other non-interest expense	416	568	1,268	1,531
Total non-interest expense	\$2,985	\$3,109	\$8,896	\$9,118

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in

(1) Qualified Affordable Housing Projects. See “Note 1—Summary of Significant Accounting Policies” for additional information. Prior periods have been recast to conform to this presentation.

(2) Includes acquisition-related costs of \$13 million and \$54 million in the third quarter and first nine months of 2014, respectively, as compared with \$37 million and \$133 million in the third quarter and first nine months of 2013, respectively. These amounts are comprised of transaction costs, legal and other professional or consulting fees, restructuring costs, and integration expense.

Non-interest expense decreased by \$124 million, or 4%, to \$3.0 billion in the third quarter of 2014, from \$3.1 billion in the third quarter of 2013. Non-interest expense decreased by \$222 million, or 2%, to \$8.9 billion in the first nine months of 2014, from \$9.1 billion in the first nine months of 2013. The decreases reflect a decline in the amortization of intangibles and a reduction in acquisition-related costs and provision for litigation matters. These were partially offset by (i) higher operating expenses attributable to growth in our commercial and auto loan portfolios; (ii) the change to include auto repossession-related expenses as a component of operating expenses (prior to January 1, 2014 these costs were reported as a component of net charge-offs); and (iii) higher marketing expenses associated with loan growth, partially offset by lower bankcard, regulatory and other fee assessments and communication and data processing expenses.

Income Taxes

We recorded income tax provisions of \$536 million (32.3% effective income tax rate) and \$1.7 billion (32.9% effective income tax rate) in the third quarter and first nine months of 2014, respectively, compared to income tax provisions of \$575 million (34.0% effective income tax rate) and \$1.7 billion (33.4% effective income tax rate) in the third quarter and first nine months of 2013, respectively. The decrease in our effective income tax rate in the third quarter of 2014 from the third quarter of 2013, was primarily attributable to increased tax credits and tax exempt income, as well as the absence of \$19 million in discrete tax expense that occurred in the third quarter of 2013. The decrease in our effective income tax rate in the first nine months of 2014 from the first nine months of 2013 was

primarily attributable to increased tax credits and tax exempt income, and certain state tax rate reductions, partially offset by increased discrete tax expense. Our effective income tax rate, excluding the impact of discrete tax items discussed above, was 32.3% and 32.4% in the third quarter and first nine months of 2014, and 32.8%, and 33.0% in the third quarter and first nine months of 2013, respectively.

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We provide additional information on items affecting our income taxes and effective tax rate in our 2013 Form 10-K in “Note 17—Income Taxes.”

Loss from Discontinued Operations, Net of Tax

Loss from discontinued operations reflects ongoing costs, which primarily consist of mortgage loan repurchase representation and warranty charges, related to the mortgage origination operations of GreenPoint Mortgage Funding, Inc.’s (“GreenPoint”) wholesale mortgage banking unit that we closed in 2007. Loss from discontinued operations, net of tax, was \$44 million and \$24 million for the third quarter and first nine months of 2014, respectively, compared to a loss from discontinued operations of \$13 million and \$210 million for the third quarter and first nine months of 2013, respectively. The pre-tax portions of the net provision for mortgage representation and warranty losses recognized on our consolidated statements of income as a component of discontinued operations were provisions of \$70 million (\$44 million net of tax) and \$34 million (\$21 million net of tax) in the third quarter and first nine months of 2014, respectively, and provisions of \$9 million (\$6 million net of tax) and \$303 million (\$190 million net of tax) in the third quarter and first nine months of 2013, respectively.

We provide additional information on the net provision for mortgage representation and warranty losses and the related reserve for representation and warranty claims in “Consolidated Balance Sheets Analysis—Mortgage Representation and Warranty Reserve” and “Note 14—Commitments, Contingencies, Guarantees, and Others.”

BUSINESS SEGMENT FINANCIAL PERFORMANCE

Our principal operations are currently organized into three major business segments, which are defined based on the products and services provided or the type of customer served: Credit Card, Consumer Banking and Commercial Banking. The operations of acquired businesses have been integrated into our existing business segments. Certain activities that are not part of a segment, such as management of our corporate investment portfolio and asset/liability management by our centralized Corporate Treasury group, are included in the Other category.

The results of our individual businesses, which we report on a continuing operations basis, reflect the manner in which management evaluates performance and makes decisions about funding our operations and allocating resources. We provide additional information on the allocation methodologies used to derive our business segment results in “Note 19—Business Segments” in our 2013 Form 10-K.

We refer to the business segment results derived from our internal management accounting and reporting process as our “managed” presentation, which differs in some cases from our reported results prepared based on U.S. GAAP. There is no comprehensive authoritative body of guidance for management accounting equivalent to U.S. GAAP; therefore, the managed presentation of our business segment results may not be comparable to similar information provided by other financial service companies. In addition, our individual business segment results should not be used as a substitute for comparable results determined in accordance with U.S. GAAP.

Below we summarize our business segment results for the third quarter and first nine months of 2014 and 2013 and provide a comparative discussion of these results. We also discuss changes in our financial condition and credit performance statistics as of September 30, 2014, compared with December 31, 2013. We provide a reconciliation of our total business segment results to our reported consolidated results in “Note 13—Business Segments.” Additionally, we provide information on the outlook for each of our business segments as described above under “Executive Summary and Business Outlook.”

Credit Card Business

The primary sources of revenue for our Credit Card business are interest income, fees collected from customers and interchange fees. Expenses primarily consist of the provision for credit losses, operating costs such as salaries and associate benefits, occupancy and equipment, professional services, communications and data processing expenses and marketing expenses. Rewards costs are generally netted against interchange fees.

Our Credit Card business generated net income from continuing operations of \$624 million and \$2.0 billion in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$694 million and \$2.1 billion in the third quarter and first nine months of 2013, respectively.

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Table 7 summarizes the financial results of our Credit Card business, which is comprised of Domestic Card and International Card, and displays selected key metrics for the periods indicated.

Table 7: Credit Card Business Results

(Dollars in millions)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2014	2013	Change	2014	2013	Change
Selected income statement data:						
Net interest income	\$2,627	\$2,757	(5)%	\$7,613	\$8,391	(9)%
Non-interest income	846	834	1	2,470	2,487	(1)
Total net revenue ⁽¹⁾	3,473	3,591	(3)	10,083	10,878	(7)
Provision for credit losses	787	617	28	1,894	2,073	(9)
Non-interest expense	1,730	1,904	(9)	5,175	5,571	(7)
Income from continuing operations before income taxes	956	1,070	(11)	3,014	3,234	(7)
Income tax provision	332	376	(12)	1,054	1,135	(7)
Income from continuing operations, net of tax	\$624	\$694	(10)	\$1,960	\$2,099	(7)
Selected performance metrics:						
Average loans held for investment ⁽²⁾	\$79,494	\$77,729	2	\$78,005	\$79,523	(2)
Average yield on loans held for investment ⁽³⁾	14.65	% 15.72	% (107) bps	14.44	% 15.60	% (116) bps
Total net revenue margin ⁽⁴⁾	17.48	18.48	(100)	17.24	18.24	(100)
Net charge-offs	\$572	\$734	(22)%	\$2,037	\$2,506	(19)%
Net charge-off rate	2.88	% 3.78	% (90) bps	3.48	% 4.20	% (72) bps
Card loan premium amortization and other intangible accretion ⁽⁵⁾	\$18	\$45	(60)%	\$86	\$159	(46)%
PCCR intangible amortization	90	106	(15)	282	332	(15)
Purchase volume ⁽⁶⁾	57,474	50,943	13	161,266	146,829	10
(Dollars in millions)	September 30, December 31,		Change			
	2014	2013				
Selected period-end data:						
Loans held for investment ⁽²⁾	\$80,631	\$81,305	(1)%			
30+ day performing delinquency rate	3.22	% 3.46	% (24) bps			
30+ day delinquency rate	3.29	3.54	(25)			
Nonperforming loan rate	0.09	0.11	(2)			
Allowance for loan and lease losses	\$3,057	\$3,214	(5)%			
Allowance coverage ratio ⁽⁷⁾	3.79	% 3.95	% (16) bps			

We recognize billed finance charges and fee income on open-ended loans in accordance with the contractual provisions of the credit arrangements and estimate the uncollectible amount on a quarterly basis. The estimated uncollectible amount of billed finance charges and fees is reflected as a reduction in revenue and is not included in our net charge-offs. Total net revenue was reduced by \$164 million and \$480 million in the third quarter and first nine months of 2014, respectively, and by \$154 million and \$611 million in the third quarter and first nine months of 2013, respectively, for the estimated uncollectible amount of billed finance charges and fees. The finance charge and fee reserve totaled \$218 million and \$190 million as of September 30, 2014 and December 31, 2013, respectively.

(1)

- (2) Period-end loans held for investment and average loans held for investment include accrued finance charges and fees, net of the estimated uncollectible amount.

Calculated by dividing annualized interest income for the period by average loans held for investment during the period. Annualized interest income excludes various allocations including funds transfer pricing that assigns

- (3) certain balance sheet assets, deposits and other liabilities and their related revenue and expenses attributable to each business segment. The transfer of the Best Buy Stores, L.P. (“Best Buy”) loan portfolio to held for sale resulted in an increase in the average yield for Credit Card of 110 and 119 basis points in the third quarter and first nine months of 2013, respectively. The sale of the Best Buy loan portfolio was completed on September 6, 2013.

Calculated by dividing annualized total net revenue for the period by average loans held for investment during the period for the specified loan category. Annualized interest income also includes interest income on loans held for

- (4) sale. The transfer of the Best Buy loan portfolio from loans held for investment to loans held for sale resulted in an increase in the net revenue margin for the total Credit Card business of 123 and 134 basis points in the third quarter and first nine months of 2013, respectively.

Represents the net reduction in interest income attributable to the amortization of premiums on purchased loans

- (5) accounted for based on contractual cash flows and the accretion of other intangibles associated with the 2012 U.S. card acquisition.

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- (6) Consists of credit card purchase transactions, net of returns for the period for both loans classified as held for investment and loans classified as held for sale. Excludes cash advance and balance transfer transactions.
- (7) Calculated by dividing the allowance for loan and lease losses as of the end of the period by period-end loans held for investment.

Key factors affecting the results of our Credit Card business for the third quarter and first nine months of 2014, compared with the third quarter and first nine months of 2013, and changes in financial condition and credit performance between September 30, 2014 and December 31, 2013 include the following:

Net Interest Income: Net interest income decreased by \$130 million, or 5%, in the third quarter of 2014 from the third quarter of 2013, to \$2.6 billion, and by \$778 million, or 9%, in the first nine months of 2014 from the first nine months of 2013, to \$7.6 billion. The decrease in net interest income was primarily driven by the Portfolio Sale in the third quarter of 2013.

Non-Interest Income: Non-interest income increased by \$12 million, or 1%, in the third quarter of 2014 from the third quarter of 2013, to \$846 million, and decreased by \$17 million, or 1%, in the first nine months of 2014 from the first nine months of 2013, to \$2.5 billion. The decrease in the first nine months of 2014 compared to the first nine months of 2013 was largely due to a reduction in service charges and other customer-related fees, partially offset by increased interchange fees, net driven by higher purchase volume.

Provision for Credit Losses: The provision for credit losses increased by \$170 million, or 28%, in the third quarter of 2014 from the third quarter of 2013, to \$787 million, and decreased by \$179 million, or 9%, in the first nine months of 2014 from the first nine months of 2013, to \$1.9 billion. The increase in the third quarter of 2014 was due to a build in the allowance for loan and lease losses in the Domestic Card business driven by higher loan volumes and higher delinquencies, partially offset by lower net charge-offs. The decrease in the provision for credit losses for the the first nine months of 2014 compared to the first nine months of 2013, was driven primarily by lower net charge-offs, which was a result of improved credit, partially offset by a smaller release of our allowance for loan and lease losses.

Non-Interest Expense: Non-interest expense decreased by \$174 million, or 9%, in the third quarter of 2014 from the third quarter of 2013, to \$1.7 billion, and decreased by \$396 million, or 7%, in the first nine months of 2014 from the first nine months of 2013, to \$5.2 billion. The decrease in the third quarter and first nine months of 2014 was largely due to lower acquisition-related costs, lower operating expenses driven by the Portfolio Sale, lower provision for litigation matters and operating efficiencies. Non-interest expense also included purchased credit card relationship (“PCCR”) intangible amortization of \$282 million in the first nine months of 2014, compared with \$332 million in the first nine months of 2013.

Loans Held for Investment: Period-end loans held for investment decreased by \$674 million, or 1%, to \$80.6 billion as of September 30, 2014, from \$81.3 billion as of December 31, 2013. This decrease was largely due to seasonality partially offset by growth in the domestic card loan portfolio in the second and third quarters of 2014.

Net Charge-off and Delinquency Statistics: Our reported net charge-off rate decreased to 2.88% and 3.48% in the third quarter and first nine months of 2014, respectively, from 3.78% and 4.20% in the third quarter and first nine months of 2013, respectively. The extremely low net charge-off rate in the third quarter 2014, based on our historical trends, was largely due to continued economic improvement and portfolio seasoning. In addition, the decrease in net charge-offs are driven by low delinquency inventories in the first nine months of 2014 compared to the first nine months of 2013. The 30+ day delinquency rate decreased to 3.29% as of September 30, 2014, from 3.54% as of December 31, 2013 and 3.60% as of September 30, 2013.

Domestic Card Business

Domestic Card generated net income from continuing operations of \$550 million and \$1.8 billion in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$644 million and \$1.9 billion in the third quarter and first nine months of 2013, respectively. Domestic Card accounted for 90% of total net revenues in the third quarter and first nine months of 2014 and 2013, for our Credit Card business.

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Table 7.1 summarizes the financial results for Domestic Card and displays selected key metrics for the periods indicated.

Table 7.1: Domestic Card Business Results

(Dollars in millions)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2014	2013	Change	2014	2013	Change
Selected income statement data:						
Net interest income	\$2,361	\$2,492	(5)%	\$6,809	\$7,584	(10)%
Non-interest income	763	749	2	2,233	2,210	1
Total net revenue ⁽¹⁾	3,124	3,241	(4)	9,042	9,794	(8)
Provision for credit losses	738	529	40	1,728	1,823	(5)
Non-interest expense	1,530	1,713	(11)	4,588	4,981	(8)
Income from continuing operations before income taxes	856	999	(14)	2,726	2,990	(9)
Income tax provision	306	355	(14)	974	1,064	(8)
Income from continuing operations, net of tax	\$550	\$644	(15)	\$1,752	\$1,926	(9)
Selected performance metrics:						
Average loans held for investment ⁽²⁾	\$71,784	\$69,947	3	\$70,331	\$71,525	(2)
Average yield on loans held for investment ⁽³⁾	14.46	% 15.65	% (119) bps	14.20	% 15.54	% (134) bps
Total net revenue margin ⁽⁴⁾	17.41	18.53	(112)	17.14	18.26	(112)
Net charge-offs	\$508	\$642	(21)%	\$1,818	\$2,218	(18)%
Net charge-off rate	2.83	% 3.67	% (84) bps	3.45	% 4.14	% (69) bps
Card loan premium amortization and other intangible accretion ⁽⁵⁾	\$18	\$45	(60)%	\$86	\$159	(46)%
PCCR intangible amortization	90	\$106	(15)	282	332	(15)
Purchase volume ⁽⁶⁾	53,690	47,420	13	150,482	136,524	10
(Dollars in millions)	September 30, December 31,		Change			
	2014	2013				
Selected period-end data:						
Loans held for investment ⁽²⁾	\$73,143	\$73,255	—	%		
30+ day delinquency rate	3.21	% 3.43	% (22) bps			
Allowance for loan and lease losses	\$2,746	\$2,836	(3)%			
Allowance coverage ratio ⁽⁷⁾	3.75	% 3.87	% (12) bps			

We recognize billed finance charges and fee income on open-ended loans in accordance with the contractual provisions of the credit arrangements and estimate the uncollectible amount on a quarterly basis. The estimated uncollectible amount of billed finance charges and fees is reflected as a reduction in revenue and is not included in our net charge-offs.

(2) Period-end loans held for investment and average loans held for investment include accrued finance charges and fees, net of the estimated uncollectible amount.

(3) Calculated by dividing annualized interest income for the period by average loans held for investment during the period for the specified loan category. Annualized interest income includes interest income on loans held for sale. The transfer of the Best Buy loan portfolio from loans held for investment to loans held for sale resulted in an increase in the average yield for the Domestic Card business of 121 and 131 basis points in the third quarter and

first nine months of 2013, respectively.

Calculated by dividing annualized total net revenue for the period by average loans held for investment during the period. Annualized interest income excludes various allocations including funds transfer pricing that assigns

(4) certain balance sheet assets, deposits and other liabilities and their related revenue and expenses attributable to each business segment. The transfer of the Best Buy loan portfolio from loans held for investment to loans held for sale resulted in an increase in the net revenue margin for the Domestic Card business of 136 and 148 basis points in the third quarter and first nine months of 2013, respectively.

(5) Represents the net reduction in interest income attributable to the amortization of premiums on purchased loans accounted for based on contractual cash flows and the accretion of other intangibles associated with the 2012 U.S. card acquisition.

(6) Consists of domestic card purchase transactions, net of returns, for the period for both loans classified as held for investment and loans classified as held for sale. Excludes cash advance and balance transfer transactions.

(7) Calculated by dividing the allowance for loan and lease losses as of the end of the period by period-end loans held for investment.

Because our Domestic Card business accounts for the substantial majority of our Credit Card business, the key factors driving the results for this division are similar to the key factors affecting our total Credit Card business. The primary drivers of the decline in net income for our Domestic Card business in the third quarter and first nine months of 2014, compared with the third quarter and first nine months of 2013, were a decrease in revenue primarily driven by the Portfolio Sale in the third quarter of 2013 and

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a higher provision for credit losses, partially offset by lower acquisition-related costs and provision for litigation matters, as well as lower operating expenses attributable to the Portfolio Sale in 2013 and operating efficiencies. The slight decrease in period-end loans held for investment from December 31, 2013 was primarily due to seasonal decreases in the first quarter of 2014, partially offset by growth in the second and third quarters of 2014.

International Card Business

International Card generated net income from continuing operations of \$74 million and \$208 million in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$50 million and \$173 million in the third quarter and first nine months of 2013, respectively. International Card accounted for 10% of total net revenues in the third quarter and first nine months of 2014 and 2013, for our Credit Card business. Table 7.2 summarizes the financial results for International Card and displays selected key metrics for the periods indicated.

Table 7.2: International Card Business Results

(Dollars in millions)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2014	2013	Change	2014	2013	Change
Selected income statement data:						
Net interest income	\$266	\$265	— %	\$804	\$807	— %
Non-interest income	83	85	(2)	237	277	(14)
Total net revenue	349	350	—	1,041	1,084	(4)
Provision for credit losses	49	88	(44)	166	250	(34)
Non-interest expense	200	191	5	587	590	(1)
Income from continuing operations before income taxes	100	71	41	288	244	18
Income tax provision	26	21	24	80	71	13
Income from continuing operations, net of tax	\$74	\$50	48	\$208	\$173	20
Selected performance metrics:						
Average loans held for investment ⁽¹⁾	\$7,710	\$7,782	(1)	\$7,674	\$7,998	(4)
Average yield on loans held for investment ⁽²⁾	16.42	% 16.35	% 7 bps	16.60	% 16.17	% 43 bps
Total net revenue margin ⁽³⁾	18.13	17.99	14	18.09	18.07	2
Net charge-offs	\$64	\$92	(30)%	\$219	\$288	(24)%
Net charge-off rate	3.32	% 4.71	% (139)bps	3.81	% 4.79	% (98)bps
Purchase volume ⁽⁴⁾	\$3,784	\$3,523	7 %	\$10,784	\$10,305	5 %
(Dollars in millions)	September 30, December 31,		Change			
	2014	2013				
Selected period-end data:						
Loans held for investment ⁽¹⁾	\$7,488	\$8,050	(7)%			
30+ day performing delinquency rate	3.34	% 3.71	% (37)bps			
30+ day delinquency rate	4.08	4.56	(48)			
Nonperforming loan rate	0.98	1.10	(12)			
Allowance for loan and lease losses	\$311	\$378	(18)%			
Allowance coverage ratio ⁽⁵⁾	4.15	% 4.70	% (55)bps			

(1) Period-end loans held for investment and average loans held for investment include accrued finance charges and fees, net of the estimated uncollectible amount.

- Calculated by dividing annualized interest income for the period by average loans held for investment during the period. Annualized interest income excludes various allocations including funds transfer pricing that assigns certain balance sheet assets, deposits and other liabilities and their related revenue and expenses attributable to each business segment.
- (2) Calculated by dividing annualized total net revenue for the period by average loans held for investment during the period.
 - (3) Consists of international card purchase transactions, net of returns for the period. Excludes cash advance and balance transfer transactions.
 - (4) Calculated by dividing the allowance for loan and lease losses as of the end of the period by period-end loans held for investment.
 - (5)

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The increase in net income in the third quarter and first nine months of 2014 compared to the third quarter and first nine months of 2013 was primarily due to a reduction in the provision for credit losses attributable to lower net charge-offs, reflecting the improvement in the credit environment in Canada and the U.K.

Consumer Banking Business

The primary sources of revenue for our Consumer Banking business are net interest income from loans and deposits and non-interest income from service charges and customer-related fees. Expenses primarily consist of the provision for credit losses, ongoing operating costs, such as salaries and associate benefits, occupancy and equipment costs, professional services, communications and data processing expenses, as well as marketing expenses.

Our Consumer Banking business generated net income from continuing operations of \$289 million and \$953 million in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$345 million and \$1.2 billion in the third quarter and first nine months of 2013, respectively.

Table 8 summarizes the financial results of our Consumer Banking business and displays selected key metrics for the periods indicated.

Table 8: Consumer Banking Business Results

(Dollars in millions)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2014	2013	Change	2014	2013	Change
Selected income statement data:						
Net interest income	\$1,425	\$1,481	(4)%	\$4,289	\$4,437	(3)%
Non-interest income	179	184	(3)	499	554	(10)
Total net revenue	1,604	1,665	(4)	4,788	4,991	(4)
Provision for credit losses	198	202	(2)	481	444	8
Non-interest expense	956	927	3	2,824	2,727	4
Income from continuing operations before income taxes	450	536	(16)	1,483	1,820	(19)
Income tax provision	161	191	(16)	530	648	(18)
Income from continuing operations, net of tax	\$289	\$345	(16)	\$953	\$1,172	(19)
Selected performance metrics:						
Average loans held for investment: ⁽¹⁾						
Auto	\$35,584	\$30,157	18	\$33,993	\$28,780	18
Home loan	31,859	37,852	(16)	33,258	40,450	(18)
Retail banking	3,605	3,655	(1)	3,616	3,721	(3)
Total consumer banking	\$71,048	\$71,664	(1)	\$70,867	\$72,951	(3)
Average yield on loans held for investment: ⁽²⁾	6.18	% 6.21	% (3) bps	6.19	% 6.04	% 15 bps
Average deposits	\$168,407	\$169,082	—	% \$168,925	\$170,294	(1)%
Average deposit interest rate	0.58	% 0.63	% (5) bps	0.58	% 0.64	% (6) bps
Core deposit intangible amortization	\$26	\$34	(24)%	\$84	\$106	(21)%
Net charge-offs	190	170	12	460	423	9
Net charge-off rate	1.07	% 0.95	% 12 bps	0.87	% 0.77	% 10 bps
Net charge-off rate (excluding Acquired Loans)	1.65	1.64	1	1.37	1.40	(3)
Auto loan originations	\$5,410	\$4,752	14	% \$15,513	\$13,066	19

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(Dollars in millions)	September 30, 2014	December 31, 2013	Change	
Selected period-end data:				
Loans held for investment: ⁽¹⁾				
Auto	\$36,254	\$31,857	14	%
Home loan	31,203	35,282	(12))
Retail banking	3,604	3,623	(1))
Total consumer banking	\$71,061	\$70,762	—	
30+ day performing delinquency rate	3.22	% 3.20	% 2	bps
30+ day performing delinquency rate (excluding Acquired Loans) ⁽³⁾	4.91	5.32	(41))
30+ day delinquency rate	3.82	3.89	(7))
30+ day delinquency rate (excluding Acquired Loans) ⁽³⁾	5.82	6.47	(65))
Nonperforming loans rate	0.73	0.86	(13))
Nonperforming loans rate (excluding Acquired Loans) ⁽³⁾	1.12	1.44	(32))
Nonperforming asset rate ⁽⁴⁾	1.01	1.12	(11))
Nonperforming asset rate (excluding Acquired Loans) ⁽³⁾	1.53	1.86	(33))
Allowance for loan and lease losses	\$772	\$752	3	%
Allowance coverage ratio ⁽⁵⁾	1.09	% 1.06	% 3	bps
Deposits	\$167,624	\$167,652	—	%
Loans serviced for others	7,041	7,665	(8))

(1) Includes Acquired Loans with carrying values of \$24.4 billion and \$28.2 billion as of September 30, 2014 and December 31, 2013, respectively. The average balance of Consumer Banking loans held for investment, excluding Acquired Loans, was \$46.2 billion and \$41.4 billion in the third quarter of 2014 and 2013, respectively, and \$44.7 billion and \$40.3 billion in the first nine months of 2014 and 2013, respectively.

(2) Calculated by dividing annualized interest income for the period by average loans held for investment during the period. Annualized interest income excludes various allocations including funds transfer pricing that assigns certain balance sheet assets, deposits and other liabilities and their related revenue and expenses attributable to each business segment.

(3) Calculation of ratio adjusted to exclude the impact from Acquired Loans. See “Credit Risk Profile” and “Note 4—Loans” for additional information on the impact of Acquired Loans on our credit quality metrics.

(4) Calculated by dividing nonperforming assets as of the end of the period by the sum of period-end loans held for investment, foreclosed properties, and other foreclosed assets.

(5) Calculated by dividing the allowance for loan and lease losses as of the end of the period by period-end loans held for investment.

Key factors affecting the results of our Consumer Banking business for the third quarter and first nine months of 2014, compared with the third quarter and first nine months of 2013, and changes in financial condition and credit performance between September 30, 2014 and December 31, 2013 include the following:

Net Interest Income: Net interest income decreased by \$56 million, or 4%, in the third quarter of 2014 from the third quarter of 2013, to \$1.4 billion, and by \$148 million, or 3%, in the first nine months of 2014 from the first nine months of 2013, to \$4.3 billion. The decrease in net interest income was primarily attributable to compression in deposit spreads in retail banking, partially offset by higher net interest income generated by growth in our auto loan portfolio.

Consumer Banking yields remained relatively flat at 6.2% when comparing the third quarter of 2014 to the third quarter of 2013 and increased in the first nine months of 2014 to 6.2%, as compared to 6.0% in the first nine months of 2013. The increase in the first nine months of 2014 from the first nine months of 2013 was driven by changes in the product mix in Consumer Banking as a result of growth in our auto loan portfolio and the run-off of the acquired home loan portfolio. The increase in our auto loans in relation to our total consumer banking loan portfolio drove an increase in the total Consumer Banking yield, even as the average yield on auto loans decreased to 8.5% in the third quarter of 2014 as compared to 9.7% in the third quarter of 2013, and decreased to 8.7% in the first nine months of 2014, as compared to 10.0% in the first nine months of 2013. This decrease was primarily attributable to a shift to a higher portion of prime auto loans and increased competition in the subprime auto business. The average yield on home loans was 3.8% and 3.7% in the third quarter and first nine months of 2014, respectively, compared to 3.5% and 3.3% in the third quarter and first nine months of 2013, respectively. The higher yield in the home loan portfolio was driven by an increase in expected cash flows as a result of credit improvement on the Acquired Loan portfolio.

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Non-Interest Income: Non-interest income decreased by \$5 million, or 3%, in the third quarter of 2014 from the third quarter of 2013, to \$179 million, and by \$55 million, or 10%, in the first nine months of 2014 from the first nine months of 2013, to \$499 million. The decrease in non-interest income for the nine months ended 2014 was attributable to a gain on sale of certain of our mortgage servicing rights (“MSR”) in the second quarter of 2013, as well as a higher provision for representation and warranty losses within the home loan portfolio.

Provision for Credit Losses: The provision for credit losses decreased by \$4 million, or 2%, in the third quarter of 2014 from the third quarter of 2013, to \$198 million, and increased by \$37 million, or 8%, in the first nine months of 2014 from the first nine months of 2013, to \$481 million. The increase in the first nine months of 2014, as compared to the first nine months of 2013, was driven by higher net charge-offs due to the growth in our auto loan portfolio and a smaller release of the allowance for loan and lease losses in the retail and home loan portfolios, offset by a smaller allowance build in the auto loan portfolio.

Non-Interest Expense: Non-interest expense increased by \$29 million, or 3%, in the third quarter of 2014 from the third quarter of 2013, to \$956 million, and by \$97 million, or 4%, in the first nine months of 2014 from the first nine months of 2013, to \$2.8 billion. The increase was largely due to the growth in our auto loan portfolio and to a smaller degree, the change to include the auto repossession-related expenses as a component of operating expenses. Prior to January 1, 2014, these costs were reported as a component of net charge-offs.

Loans Held for Investment: Period-end loans held for investment increased by \$299 million, or less than 1%, in the first nine months of 2014 to \$71.1 billion as of September 30, 2014 from \$70.8 billion as of December 31, 2013, primarily due to the growth in the auto loan portfolio, mostly offset by the run-off of our acquired home loan portfolio.

Deposits: Period-end deposits decreased by \$28 million, or less than 1%, in the first nine months of 2014 to \$167.6 billion as of September 30, 2014, from \$167.7 billion as of December 31, 2013.

Net Charge-off and Delinquency Statistics: The reported net charge-off rate increased by 12 basis points to 1.07% in the third quarter of 2014 from 0.95% in the third quarter of 2013, and increased by 10 basis points to 0.87% in the first nine months of 2014 from 0.77% in the first nine months of 2013. The increase in the net charge-off rate reflected a shift in the mix of the portfolio toward auto loans (which typically carry higher net charge-off rates than our home loan portfolio), as home loans run off. The 30+ day delinquency rate decreased to 3.82% as of September 30, 2014, from 3.89% as of December 31, 2013.

Commercial Banking Business

The primary sources of revenue for our Commercial Banking business are net interest income from loans and deposits and non-interest income from customer-related fees. Because we have some investments that generate tax-exempt income or tax credits, we make certain reclassifications to our Commercial Banking business results to present revenues on a taxable-equivalent basis. Expenses primarily consist of the provision for credit losses, ongoing operating costs, such as salaries and associate benefits, occupancy, equipment, professional services, communications and data processing expenses, as well as marketing expenses.

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in Qualified Affordable Housing Projects. The proportional amortization method amortizes the cost of the investment over the period in which we will receive tax credits and other tax benefits, and the resulting amortization is recognized as a component of income taxes attributable to continuing operations. Historically, these investments were accounted for under the equity method of accounting and the passive losses related to the investments were recognized within non-interest expense. See “Note 1—Summary of Significant Accounting Policies” for more information.

Our Commercial Banking business generated net income from continuing operations of \$182 million and \$490 million in the third quarter and first nine months of 2014, respectively, compared with net income from continuing operations of \$162 million and \$536 million in the third quarter and first nine months of 2013, respectively.

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Table 9 summarizes the financial results of our Commercial Banking business and displays selected key metrics for the periods indicated.

Table 9: Commercial Banking Business Results⁽¹⁾

(Dollars in millions)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2014	2013	Change	2014	2013	Change
Selected income statement data:						
Net interest income	\$439	\$424	4 %	\$1,296	\$1,227	6 %
Non-interest income	122	87	40	318	264	20
Total net revenue ⁽²⁾⁽³⁾	561	511	10	1,614	1,491	8
Provision (benefit) for credit losses	9	31	(71)	61	(18)	**
Non-interest expense	268	228	18	790	677	17
Income from continuing operations before income taxes	284	252	13	763	832	(8)
Income tax provision	102	90	13	273	296	(8)
Income from continuing operations, net of tax	\$182	\$162	12	\$490	\$536	(9)
Selected performance metrics:						
Average loans held for investment: ⁽⁴⁾						
Commercial and multifamily real estate	\$22,409	\$19,047	18	\$21,623	\$18,201	19
Commercial and industrial	25,512	21,491	19	24,562	20,596	19
Total commercial lending	47,921	40,538	18	46,185	38,797	19
Small-ticket commercial real estate	845	1,038	(19)	891	1,102	(19)
Total commercial banking	\$48,766	\$41,576	17	\$47,076	\$39,899	18
Average yield on loans held for investment ⁽²⁾	3.39 %	3.87 %	(48) bps	3.45 %	3.87 %	(42) bps
Average deposits	\$31,772	\$30,685	4 %	\$31,546	\$30,590	3 %
Average deposit interest rate	0.24 %	0.27 %	(3) bps	0.24 %	0.27 %	(3) bps
Core deposit intangible amortization	\$5	\$6	(17) %	\$16	\$21	(24) %
Net (recoveries) charge-offs	(6)	8	**	1	19	(95)
Net (recovery) charge-off rate	(0.05)%	0.07 %	**	0.00 %	0.06 %	(6) bps
(Dollars in millions)	September 30, 2014	December 31, 2013	Change			
Selected period-end data:						
Loans held for investment: ⁽⁴⁾						
Commercial and multifamily real estate	\$22,895	\$20,750	10 %			
Commercial and industrial	26,071	23,309	12			
Total commercial lending	48,966	44,059	11			
Small-ticket commercial real estate	822	952	(14)			
Total commercial banking	\$49,788	\$45,011	11			
Nonperforming loans rate	0.32 %	0.33 %	(1) bps			
Nonperforming asset rate ⁽⁴⁾	0.35	0.37	(2)			
	\$378	\$338	12 %			

Allowance for loan and lease
losses

Allowance coverage ratio ⁽⁵⁾	0.76	%	0.75	%	1	bps
Deposits	\$31,918		\$ 30,567		4	%
Loans serviced for others	12,559		10,786		16	

** Change is not meaningful.

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in

(1) Qualified Affordable Housing Projects. See “Note 1—Summary of Significant Accounting Policies” for additional information. Prior periods have been recast to conform to this presentation.

The average yield on loans held for investment is calculated by dividing annualized interest income for the period by average loans held for investment during the period. Annualized interest income excludes various allocations including funds transfer pricing that assigns certain balance sheet assets, deposits and other liabilities and their

(2) related revenue and expenses attributable to each business segment. Some of our tax-related commercial investments generate tax-exempt income or tax credits. Accordingly, we make certain reclassifications within our Commercial Banking business results to present revenues and yields on a taxable-equivalent basis, calculated assuming an effective tax rate approximately equal to our federal statutory tax rate of 35%.

(3) Some of our tax-related commercial investments generate tax-exempt income or tax credits. Accordingly, we make certain reclassifications within our

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Commercial Banking business results to present revenues and yields on a taxable-equivalent basis, calculated assuming an effective tax rate approximately equal to our federal statutory tax rate of 35%.

- (4) Calculated by dividing nonperforming assets as of the end of the period by the sum of period-end loans held for investment, foreclosed properties, and other foreclosed assets.
- (5) Calculated by dividing the allowance for loan and lease losses as of the end of the period by period-end loans held for investment.

Key factors affecting the results of our Commercial Banking business for the third quarter and first nine months of 2014, compared with the third quarter and first nine months of 2013, and changes in financial condition and credit performance between September 30, 2014 and December 31, 2013 include the following:

Net Interest Income: Net interest income increased by \$15 million, or 4%, in the third quarter of 2014 from the third quarter of 2013, to \$439 million, and by \$69 million, or 6%, in the first nine months of 2014 from the first nine months of 2013, to \$1.3 billion. The increase was driven by growth in commercial and multifamily real estate and commercial and industrial loans, partially offset by lower loan yields driven by market and competitive pressures.

Non-Interest Income: Non-interest income increased by \$35 million, or 40%, in the third quarter of 2014 from the third quarter of 2013, to \$122 million, and by \$54 million, or 20%, in the first nine months of 2014 from the first nine months of 2013, to \$318 million, primarily driven by increased revenue related to fee-based services and products and the Beech Street Capital acquisition.

Provision for Credit Losses: The provision for credit losses decreased by \$22 million in the third quarter of 2014 to \$9 million compared to \$31 million in the third quarter of 2013, and increased by \$79 million in the first nine months of 2014 to \$61 million from a benefit of \$18 million in the first nine months of 2013. The decrease in the third quarter of 2014, as compared to the third quarter of 2013, was primarily due to lower net charge-offs and a decrease in the reserve for unfunded lending commitments. The increase in the first nine months of 2014, as compared to the first nine months of 2013, was primarily driven by a build in the allowance for loan and lease losses due to growth in the portfolio. This was partially offset by decreases in net charge-offs and the reserve for unfunded lending commitments. The allowance for loan and lease losses and reserve for unfunded lending commitments increased by \$15 million and \$60 million in the third quarter and first nine months of 2014, respectively, compared to an increase of \$23 million and a decrease of \$38 million in the third quarter and first nine months of 2013, respectively.

Non-Interest Expense: Non-interest expense increased by \$40 million, or 18%, in the third quarter of 2014 from the third quarter of 2013, to \$268 million, and by \$113 million, or 17%, in the first nine months of 2014 from the first nine months of 2013, to \$790 million, driven by operating expenses associated with continued investments in business growth and the Beech Street Capital acquisition.

Loans Held for Investment: Period-end loans held for investment increased by \$4.8 billion, or 11%, to \$49.8 billion as of September 30, 2014 from \$45.0 billion as of December 31, 2013. The increase was driven by loan growth in the commercial and industrial and commercial and multifamily real estate businesses.

Deposits: Period-end deposits increased by \$1.3 billion, or 4%, to \$31.9 billion as of September 30, 2014, from \$30.6 billion as of December 31, 2013, driven by our strategy to deepen and expand relationships with commercial customers.

Net Charge-off Statistics: The net recovery rates were 0.05% and 0.00% in the third quarter and first nine months of 2014, respectively compared to net charge-off rates of 0.07% and 0.06% in the third quarter and first nine months of 2013, respectively. The nonperforming loans rate decreased to 0.32% as of September 30, 2014, from 0.33% as of December 31, 2013. The continued strength in the credit metrics in our Commercial Banking business reflects stable credit trends and underlying collateral values.

Other Category

Other includes unallocated amounts related to our centralized Corporate Treasury group activities, such as management of our corporate investment portfolio and asset/liability management, gains and losses on our investment securities portfolio and certain trading activities. Other also includes foreign exchange-rate fluctuations related to the revaluation of foreign currency-denominated investments; certain gains and losses on the sale and securitization of loans; unallocated corporate expenses that do not directly support the operations of the business segments or for which

the business segments are not considered financially accountable in evaluating their performance, such as certain acquisition and restructuring charges; a portion of the net provision for representation and warranty losses related to continuing operations; certain material items that are non-recurring in nature; and offsets related to certain line-item reclassifications.

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Table 10 summarizes the financial results of our Other category for the periods indicated.

Table 10: Other Results⁽¹⁾

(Dollars in millions)	Three Months Ended			Nine Months Ended September		
	September 30, 2014	2013	Change	2014	2013	Change
Selected income statement data:						
Net interest income (expense) ⁽²⁾	\$6	\$(102)	) **	\$(36)	\$(372)	) (90) %
Non-interest income	(5)	(14)	) (64) %	28	(148)) **
Total net revenue (loss)	1	(116)	) **	(8)	(520)	) (98)
Benefit for credit losses	(1)	(1)	) —	(4)	(3)	) 33
Non-interest expense	31	50	(38)	107	143	(25)
Loss from continuing operations before income taxes	(29)	(165)	) (82)	(111)	(660)	) (83)
Income tax benefit	(59)	(82)	) (28)	(161)	(332)	) (52)
Profit (loss) from continuing operations, net of tax	\$30	\$(83)	) **	\$50	\$(328)) **

**Change is not meaningful.

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in (1) Qualified Affordable Housing Projects. See “Note 1—Summary of Significant Accounting Policies” for additional information. Prior periods have been recast to conform to this presentation.

Some of our tax-related commercial investments generate tax-exempt income or tax credits, accordingly we make (2) certain reclassifications within our Commercial Banking business results to present revenues and yields on a taxable-equivalent basis, with offsetting reclassifications within the Other category, calculated assuming an effective tax rate approximately equal to our federal statutory tax rate of 35%.

Net profit from continuing operations recorded in Other was \$30 million and \$50 million in the third quarter and first nine months of 2014, respectively, compared with a net loss from continuing operations of \$83 million and \$328 million in the third quarter and first nine months of 2013, respectively. The shift to a net profit from a net loss was primarily due to higher net revenues, lower funding costs, as well as the absence of the one-time charge associated with our redemption of trust preferred securities in January 2013.

CONSOLIDATED BALANCE SHEETS ANALYSIS

Total assets increased by \$3.3 billion to \$300.2 billion as of September 30, 2014, from \$296.9 billion, as of December 31, 2013. Total liabilities increased by \$883 million to \$256.2 billion as of September 30, 2014, from \$255.3 billion as of December 31, 2013. Stockholders’ equity increased by \$2.4 billion to \$44.0 billion as of September 30, 2014 from \$41.6 billion as of December 31, 2013. The increase in stockholders’ equity was primarily attributable to our net income of \$3.4 billion in the first nine months of 2014 and \$484 million in preferred stock issuances during the first nine months of 2014, partially offset by \$1.5 billion of share repurchases under the 2014 Stock Repurchase Program and \$559 million of dividend payments.

Following is a discussion of material changes in the major components of our assets and liabilities during the first nine months of 2014. Period-end balance sheet amounts may vary from average balance sheet amounts due to liquidity and balance sheet management activities that are intended to ensure the adequacy of capital while managing our liquidity requirements for the Company and our customers and our market risk exposure in accordance with our risk appetite.

Investment Securities

Our investment portfolio consists primarily of the following: U.S. Treasury debt; U.S. agency debt and corporate debt securities guaranteed by U.S. government agencies; U.S. government sponsored enterprise or agency (“Agency”) and non-agency residential mortgage-backed securities (“RMBS”) and commercial mortgage-backed securities (“CMBS”); other asset-backed securities (“ABS”); and other investments. The carrying value of our investments in U.S. Treasury, Agency securities and other securities guaranteed by the U.S. government or agencies of the U.S. government

represented 85% and 77% of our total investment securities portfolio as of September 30, 2014 and December 31, 2013, respectively. The change in the portfolio composition is in preparation for the final rules implementing the Basel III liquidity coverage ratio, for which we provide additional information in “MD&A—Supervision and Regulation.” During the first nine months of 2014, the fair value of our investment portfolio increased by \$1.6 billion, or 3% from \$61.0 billion as of December 31, 2013, to \$62.6 billion as of September 30, 2014. This increase was primarily driven by lower interest rates.

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We had gross unrealized gains of \$874 million and gross unrealized losses of \$312 million on available-for sale investment securities as of September 30, 2014, compared with gross unrealized gains of \$799 million and gross unrealized losses of \$631 million as of December 31, 2013. The decrease in gross unrealized losses in the first nine months of 2014 was primarily driven by lower interest rates in the third quarter of 2014. Of the \$312 million in gross unrealized losses as of September 30, 2014, \$271 million was related to securities that had been in a loss position for more than 12 months. We provide information on OTTI recognized in earnings on our investment securities above in “Consolidated Results of Operations—Non-Interest Income.”

Table 11 presents the amortized cost, carrying value and fair value for the major categories of our portfolio of investment securities as of September 30, 2014 and December 31, 2013.

Table 11: Investment Securities

(Dollars in millions)	September 30, 2014		December 31, 2013	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Investment securities available for sale				
U.S. Treasury debt obligations	\$4,261	\$4,261	\$831	\$833
U.S. agency debt obligations	1	1	1	1
Corporate debt securities guaranteed by U.S. government agencies	1,001	979	1,282	1,234
RMBS:				
Agency ⁽¹⁾	20,853	20,986	21,572	21,479
Non-agency	3,024	3,497	3,165	3,600
Total RMBS	23,877	24,483	24,737	25,079
CMBS:				
Agency ⁽¹⁾	4,029	3,983	4,262	4,198
Non-agency	1,809	1,803	1,854	1,808
Total CMBS	5,838	5,786	6,116	6,006
Other ABS ⁽²⁾	3,038	3,083	7,123	7,136
Other securities ⁽³⁾	1,087	1,072	1,542	1,511
Total investment securities available for sale	\$39,103	\$39,665	\$41,632	\$41,800
(Dollars in millions)	Carrying Value	Fair Value	Carrying Value	Fair Value
Investment securities held to maturity				
Agency RMBS	\$20,349	\$21,038	\$17,443	\$17,485
Agency CMBS	1,833	1,890	1,689	1,700
Total investment securities held to maturity	\$22,182	\$22,928	\$19,132	\$19,185

(1) Agency includes Federal National Mortgage Association (“Fannie Mae”), Federal Home Loan Mortgage Corporation (“Freddie Mac”), and Government National Mortgage Association (“Ginnie Mae”).

ABS collateralized by credit card loans constituted approximately 55% and 65% of the other ABS portfolio as of September 30, 2014, and December 31, 2013, respectively, and ABS collateralized by auto dealer floor plan inventory loans and leases constituted approximately 16% and 15% of the other ABS portfolio as of September 30, 2014, and December 31, 2013, respectively. Approximately 89% of the securities in our other asset-backed security portfolio were rated AAA or its equivalent as of September 30, 2014, compared with 87% as of December 31, 2013.

(3) Includes foreign government/agency bonds, covered bonds, corporate securities, municipal securities and equity investments primarily related to activities under the Community Reinvestment Act (“CRA”).

Credit Ratings

Our portfolio of investment securities continues to be concentrated in securities that generally have high credit ratings and low credit risk, such as securities issued and guaranteed by the U.S. Treasury and Agencies. Approximately 92% of our total investment securities portfolio was rated AA+ or its equivalent, or better as of both September 30, 2014 and December 31, 2013, while approximately 6% and 5% was below investment grade as of September 30, 2014 and December 31, 2013, respectively. We

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categorize the credit ratings of our investment securities based on the lowest credit rating as issued by the following rating agencies: Standard & Poor's Ratings Services ("S&P"), Moody's Investors Service ("Moody's") and Fitch Ratings ("Fitch").

Table 12 provides information on the credit ratings of our non-agency RMBS, non-agency CMBS, other ABS and other securities in our portfolio as of September 30, 2014 and December 31, 2013.

Table 12: Non-Agency Investment Securities Credit Ratings

(Dollars in millions)	September 30, 2014				December 31, 2013			
	Amortized Cost	AAA	Other Investment Grade	Below Investment Grade or Not Rated	Amortized Cost	AAA	Other Investment Grade	Below Investment Grade or Not Rated
Non-agency RMBS	\$3,024	—	% 3	% 97	% \$3,165	—	% 4	% 96
Non-agency CMBS	1,809	100	—	—	1,854	99	1	—
Other ABS	3,038	89	6	5	7,123	87	12	1
Other securities	1,087	2	88	10	1,542	9	82	9

For additional information on our investment securities, see "Note 3—Investment Securities."

Loans Held for Investment

Total loans held for investment ("HFI") consists of unrestricted loans and restricted loans held in our securitization trusts. Table 13 summarizes our portfolio of loans held for investment by business segment, net of the allowance for loan and lease losses, as of September 30, 2014 and December 31, 2013.

Table 13: Loans Held for Investment

(Dollars in millions)	September 30, 2014			December 31, 2013		
	Loans	Allowance	Net Loans	Loans	Allowance	Net Loans
Credit Card	\$80,631	\$3,057	\$77,574	\$81,305	\$3,214	\$78,091
Consumer Banking	71,061	772	70,289	70,762	752	70,010
Commercial Banking	49,788	378	49,410	45,011	338	44,673
Other	112	5	107	121	11	110
Total	\$201,592	\$4,212	\$197,380	\$197,199	\$4,315	\$192,884

Period-end loans held for investment increased by \$4.4 billion, or 2.2%, in the the first nine months of 2014. The increase was due to commercial and industrial and commercial and multifamily real estate loan growth in our Commercial Banking business, and continued strong auto loan originations outpacing the run-off of the acquired home loan portfolio in our Consumer Banking business. Overall, there was a decline in our credit card loan portfolio primarily due to seasonality, partially offset by growth in the second and third quarters of 2014.

We provide additional information on the composition of our loan portfolio and credit quality below in "Credit Risk Profile," "MD&A—Consolidated Results of Operations" and "Note 4—Loans."

Loans Held for Sale

Loans held for sale, which are carried at lower of cost or fair value, increased to \$427 million as of September 30, 2014, from \$218 million as of December 31, 2013. The increase was primarily driven by higher originations in the Commercial Banking business and timing of sales of loans.

Deposits

Our deposits represent our largest source of funding for our operations, providing a consistent source of low-cost funds. Total deposits decreased by \$259 million to \$204.3 billion as of September 30, 2014, from \$204.5 billion as of December 31, 2013. The decrease in deposits was primarily driven by the run-off of certain deposits, which was partially offset by the growth in our Consumer Banking and Commercial Banking businesses. We provide information on the composition of our deposits, average outstanding balances, interest expense and yield below in "Liquidity Risk Profile."

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Securitized Debt Obligations

Securitized debt obligations increased by \$219 million during the first nine months of 2014, to \$10.5 billion as of September 30, 2014, from \$10.3 billion as of December 31, 2013. The increase was driven by issuances of \$3.0 billion of securitized debt obligations during the first nine months of 2014, partially offset by maturities of \$2.8 billion. We provide additional information on our borrowings below in “Liquidity Risk Profile.”

Other Debt

Other debt, which consists primarily of federal funds purchased and securities loaned or sold under agreements to repurchase, senior and subordinated notes and FHLB advances, totaled \$31.7 billion as of September 30, 2014, of which \$12.1 billion represented short-term borrowings and \$19.6 billion represented long-term debt. Other debt totaled \$30.4 billion as of December 31, 2013, of which \$16.2 billion represented short-term borrowings and \$14.2 billion represented long-term debt.

The increase in other debt of \$1.3 billion in the first nine months of 2014 was primarily attributable to the issuance of \$7.8 billion of unsecured senior notes, as well as a \$1.4 billion increase in federal funds purchased and securities loaned or sold under agreements to repurchase, partially offset by net maturities of \$5.4 billion of FHLB advances and maturities of \$2.4 billion in unsecured senior notes. We provide additional information on our borrowings below in “Liquidity Risk Profile” and in “Note 8—Deposits and Borrowings.”

Mortgage Representation and Warranty Reserve

We acquired three subsidiaries that originated residential mortgage loans and sold these loans to various purchasers, including purchasers who created securitization trusts. These subsidiaries are Capital One Home Loans, LLC, which was acquired in February 2005; GreenPoint, which was acquired in December 2006 as part of the North Fork acquisition; and CCB, which was acquired in February 2009 and subsequently merged into CONA.

We have established representation and warranty reserves for losses associated with the mortgage loans sold by each subsidiary that we consider to be both probable and reasonably estimable, including both litigation and non-litigation liabilities. These reserves are reported on our consolidated balance sheets as a component of other liabilities. The reserve setting process relies heavily on estimates, which are inherently uncertain, and requires the application of judgment. We evaluate these estimates on a quarterly basis. We build our representation and warranty reserves through the provision for mortgage representation and warranty losses, which we report on our consolidated statements of income as a component of non-interest income for loans originated and sold by CCB and Capital One Home Loans, LLC and as a component of discontinued operations for loans originated and sold by GreenPoint. In establishing the representation and warranty reserves, we consider a variety of factors depending on the category of purchaser. The aggregate reserve for all three entities totaled \$1.1 billion as of September 30, 2014, compared with \$1.2 billion as of December 31, 2013.

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The table below summarizes changes in our representation and warranty reserve in the third quarter and first nine months of 2014 and 2013.

Table 14: Changes in Representation and Warranty Reserve⁽¹⁾

(Dollars in millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Representation and warranty repurchase reserve, beginning of period	\$1,012	\$1,156	\$1,172	\$899
Provision (benefit) for mortgage representation and warranty losses:				
Recorded in continuing operations	—	(13)	(15)	(27)
Recorded in discontinued operations	70	9	34	303
Total provision (benefit) for mortgage representation and warranty losses	70	(4)	19	276
Net realized losses	(2)	(7)	(111)	(30)
Representation and warranty repurchase reserve, end of period	\$1,080	\$1,145	\$1,080	\$1,145

⁽¹⁾ Reported on our consolidated balance sheets as a component of other liabilities.

As part of our business planning processes, we have considered various outcomes relating to the future representation and warranty liabilities of our subsidiaries that are possible but do not rise to the level of being both probable and reasonably estimable outcomes justifying an incremental accrual under applicable accounting standards. Our current best estimate of reasonably possible future losses from representation and warranty claims beyond what was in our reserve as of September 30, 2014, is approximately \$2.3 billion, a decline from our estimate of \$2.6 billion as of December 31, 2013. The decrease in the reasonably possible estimate of representation and warranty reserve was primarily driven by legal developments.

We provide additional information related to the representation and warranty reserve, including factors that may impact the adequacy of the reserve and the ultimate amount of losses incurred by our subsidiaries, in “Note 14—Commitments, Contingencies, Guarantees, and Others.”

OFF-BALANCE SHEET ARRANGEMENTS AND VARIABLE INTEREST ENTITIES

In the ordinary course of business, we are involved in various types of arrangements with limited liability companies, partnerships or trusts that often involve special purpose entities and variable interest entities (“VIE”). Some of these arrangements are not recorded on our consolidated balance sheets or may be recorded in amounts different from the full contract or notional amount of the arrangements, depending on the nature or structure of, and accounting required to be applied to, the arrangement. These arrangements may expose us to potential losses in excess of the amounts recorded on our consolidated balance sheets. Our involvement in these arrangements can take many forms, including securitization and servicing activities, the purchase or sale of mortgage-backed or other asset-backed securities in connection with our home loan portfolio and loans to VIEs that hold debt, equity, real estate or other assets.

Our continuing involvement in unconsolidated VIEs primarily consists of certain mortgage loan trusts and community reinvestment and development entities. We provide a discussion of our activities related to these VIEs in “Note 6—Variable Interest Entities and Securitizations.”

CAPITAL MANAGEMENT

The level and composition of our capital are determined by multiple factors, including our consolidated regulatory capital requirements and internal risk-based capital assessments such as internal stress testing and economic capital. The level and composition of our capital may also be influenced by rating agency guidelines, subsidiary capital requirements, the business environment, conditions in the financial markets and assessments of potential future losses due to adverse changes in our business and market environments.

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Capital Standards and Prompt Corrective Action

Bank holding companies and national banks are subject to capital adequacy standards adopted by the Federal Reserve and the OCC, respectively. The capital adequacy standards set forth minimum risk-based and leverage capital requirements that are based on quantitative and qualitative measures of assets and off-balance sheet items. National banks, as insured depository institutions, are also subject to Prompt Corrective Action (“PCA”) capital regulations, which require the U.S. federal banking agencies to take “prompt corrective action” for banks that do not meet established minimum capital requirements.

In July 2013, the Federal Banking Agencies finalized a new capital rule that implements the Basel III capital accord (the “Final Basel III Capital Rules”) developed by the Basel Committee on Banking Supervision (“Basel Committee”) and certain Dodd-Frank Act capital provisions and updates the PCA capital requirements. Prior to being revised in the Final Basel III Capital Rules, the minimum risk-based capital requirements adopted by the U.S. federal banking agencies followed the Basel I framework, originally promulgated pursuant to the Basel Committee’s Basel I accord, and the advanced approaches capital rules (“Advanced Approaches”), based upon the framework originally promulgated as a result of the Basel II accord. The Final Basel III Capital Rules amended both the Basel I and Advanced Approaches frameworks, establishing a new common equity Tier 1 capital requirement and setting higher minimum capital ratio requirements. The Company refers to the amended Basel I framework as the “Basel III Standardized Approach,” and the amended Advanced Approaches framework as the “Basel III Advanced Approaches.”

At the end of 2012, the Company met one of the two independent eligibility criteria set by banking regulators for becoming subject to the Advanced Approaches capital rules. As a result, the Company has undertaken a multi-year process of implementing the Advanced Approaches regime for calculating risk-weighted assets and regulatory capital levels. Certain provisions of the Final Basel III Capital Rules began to take effect on January 1, 2014 for Advanced Approaches banking organizations, including the Company. The Company will be subject to a parallel run under Advanced Approaches during which it will calculate capital ratios under both the Basel III Standardized Approach and the Basel III Advanced Approaches, though it will continue to use the Basel III Standardized Approach for purposes of meeting regulatory capital requirements. We have notified our regulators of our intent to enter a parallel run beginning January 1, 2015. By rule, the parallel run must last at least four consecutive quarters. Therefore, the first quarter of 2016 is the earliest possible date on which the Company would use the Basel III Advanced Approaches framework in calculating its regulatory capital and risk-weighted assets for purposes of risk-based capital requirements. Consistent with the experience of other U.S. banks, it is possible that our parallel run will last longer than the four quarter minimum. Under the Dodd-Frank Act and the Final Basel III Capital Rules, organizations subject to Basel III Advanced Approaches may not hold less capital than would be required under the Basel III Standardized Approach. Therefore, even after we exit parallel run, we will continue to calculate regulatory capital and risk-weighted assets under the Basel III Standardized Approach.

As of January 1, 2014, the new minimum risk-based and leverage capital requirements for Advanced Approaches banking organizations include a common equity Tier 1 capital ratio of at least 4.0%, a Tier 1 risk-based capital ratio of at least 5.5%, a total risk-based capital ratio of at least 8.0%, and a Tier 1 leverage capital ratio of at least 4.0%. On January 1, 2015, the minimum risk-based capital ratio requirements will increase to 4.5% for the common equity Tier 1 capital ratio and to 6.0% for the Tier 1 risk-based capital ratio. The minimum requirements for the total risk-based capital ratio and the Tier 1 leverage capital ratio will not change from 2014 to 2015.

Insured depository institutions also are subject to PCA capital regulations. Under current PCA regulations, an insured depository institution is considered to be well-capitalized if it maintains a Tier 1 risk-based capital ratio of at least 6.0%, a total risk-based capital ratio of at least 10.0%, a Tier 1 leverage capital ratio of at least 5.0%, and is not subject to any written agreement, order, capital directive, or prompt corrective action directive issued by its regulator. While the Final Basel III Capital Rules increase some of the thresholds for the PCA capital categories and add the new common equity Tier 1 capital ratio to the PCA regulations, those changes are not effective until January 1, 2015.

Beginning on January 1, 2015, the well-capitalized level for the Tier 1 risk-based capital ratio will increase to 8.0%, and the well-capitalized level for the common equity Tier 1 capital ratio will be established at 6.5%. The well-capitalized levels for the total risk-based capital ratio and the Tier 1 leverage capital ratio will not change.

Prior to 2014, we also disclosed a Tier 1 common capital ratio for our bank holding company, which is a regulatory capital measure widely used by investors, analysts, rating agencies and bank regulatory agencies to assess the capital position of financial services companies. There was no mandated minimum or well-capitalized standard for the Tier 1 common capital ratio.

We disclose a non-GAAP tangible common equity ratio (“TCE ratio”) in “MD&A—Summary of Selected Financial Data.” While the TCE ratio is a capital measure widely used by investors, analysts, rating agencies, and bank regulatory agencies to assess the capital position of financial services companies, it may not be comparable to similarly titled measures reported by other companies.

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We provide information on the calculation of this ratio in “MD&A—Supplemental Tables—Table A: Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures.”

Table 15 provides a comparison of our regulatory capital ratios under the U.S. federal banking agencies’ capital adequacy standards as of September 30, 2014 and December 31, 2013. Under the Final Basel III Capital Rules, beginning on January 1, 2014, as an Advanced Approaches banking organization that has yet to enter or exit parallel run, we began using the Basel III Standardized Approach for calculating our regulatory capital, subject to applicable transition provisions. In 2014, however, we continue to use Basel I for calculating our risk-weighted assets in our regulatory capital ratios, as required under the Final Basel III Capital Rules. Beginning on January 1, 2015, we will begin using the Basel III Standardized Approach for calculating our risk-weighted assets in our regulatory capital ratios.

Table 15: Capital Ratios⁽¹⁾⁽²⁾

	September 30, 2014			December 31, 2013		
	Capital Ratio	Minimum Capital Adequacy	Well-Capitalized	Capital Ratio	Minimum Capital Adequacy	Well-Capitalized
Capital One Financial Corp:						
Common equity Tier 1 capital ⁽³⁾	12.73	% 4.00	% N/A	N/A	N/A	N/A
Tier 1 common capital ⁽⁴⁾	N/A	N/A	N/A	12.19	% N/A	N/A
Tier 1 risk-based capital ⁽⁵⁾	13.31	% 5.50	% 6.00	% 12.57	4.00	% 6.00
Total risk-based capital ⁽⁶⁾	15.24	8.00	10.00	14.69	8.00	10.00
Tier 1 leverage ⁽⁷⁾	10.64	4.00	N/A	10.06	4.00	N/A
Capital One Bank (USA), N.A.:						
Common equity Tier 1 capital ⁽³⁾	11.89	4.00	N/A	N/A	N/A	N/A
Tier 1 risk-based capital ⁽⁵⁾	11.89	5.50	6.00	% 11.47	% 4.00	% 6.00
Total risk-based capital ⁽⁶⁾	15.23	8.00	10.00	14.90	8.00	10.00
Tier 1 leverage ⁽⁷⁾	9.88	4.00	5.00	10.21	4.00	5.00
Capital One, N.A.:						
Common equity Tier 1 capital ⁽³⁾	12.80	4.00	N/A	N/A	N/A	N/A
Tier 1 risk-based capital ⁽⁵⁾	12.80	5.50	6.00	% 12.67	% 4.00	% 6.00
Total risk-based capital ⁽⁶⁾	13.87	8.00	10.00	13.76	8.00	10.00
Tier 1 leverage ⁽⁷⁾	9.10	4.00	5.00	8.96	4.00	5.00

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in
⁽¹⁾ Qualified Affordable Housing Projects. See “Note 1—Summary of Significant Accounting Policies” for additional information. Prior periods have been recast to conform to this presentation.

Capital ratios are calculated based on the Basel I capital framework as of December 31, 2013 and are calculated based on the Basel III Standardized Approach framework, subject to applicable transition provisions, as of
⁽²⁾ September 30, 2014. Capital ratios that are not applicable are denoted by “N/A.” See “MD&A—Supplemental Tables—Table A: Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures” for additional information.

⁽³⁾ Common equity Tier 1 capital ratio is a regulatory capital measure under Basel III calculated based on common equity Tier 1 capital divided by risk-weighted assets.

⁽⁴⁾ Tier 1 common capital ratio is a regulatory capital measure under Basel I calculated based on Tier 1 common capital divided by Basel I risk-weighted assets.

⁽⁵⁾ Tier 1 risk-based capital ratio is a regulatory capital measure calculated based on Tier 1 capital divided by risk-weighted assets.

⁽⁶⁾ Total risk-based capital ratio is a regulatory capital measure calculated based on total risk-based capital divided by risk-weighted assets.

(7) Tier 1 leverage ratio is a regulatory capital measure calculated based on Tier 1 capital divided by average assets, after certain adjustments.

Capital One Financial Corporation exceeded U.S. federal banking agencies' minimum capital requirements and the Banks exceeded minimum regulatory requirements and were "well-capitalized" under PCA requirements as of September 30, 2014 and December 31, 2013. Our common equity Tier 1 capital ratio, as calculated under the Basel III Standardized Approach, subject to transition provisions, was 12.73% as of September 30, 2014. Our Tier 1 common capital ratio, as calculated under Basel I, was 12.19% as of December 31, 2013. These numbers are not directly comparable due to methodological differences in the calculation of the ratios and the transition requirements under the Final Basel III Capital Rules. For purposes of our capital plan to be completed for the 2015 CCAR Cycle, we will be assessed on our ability to maintain specified minimum levels of capital under our currently effective Basel III Standardized Approach regime, along with a Tier 1 common ratio of 5.0% on a pro forma basis, as calculated under Basel I, under expected and stressful conditions. We estimate that our Tier 1 common ratio, as calculated under Basel I, was

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approximately 12.72% as of September 30, 2014. See “MD&A—Supplemental Tables—Table A: Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures” for additional information about our Tier 1 common ratio, as calculated under Basel I.

As described above, we currently are using the Basel III Standardized Approach for calculating our regulatory capital, subject to transition provisions. The calculation of our Basel III Standardized Approach common equity Tier 1 capital under the Final Basel III Capital Rules includes additional adjustments and deductions not included in the Tier 1 common capital calculation under Basel I, such as the inclusion of the unrealized gains and losses on available-for-sale investment securities included in AOCI and adjustments related to intangibles. The adjustments are phased-in at 20% for 2014, 40% for 2015, 60% for 2016, 80% for 2017 and 100% for 2018. Also as described above, we continue to use Basel I for calculating our risk-weighted assets in our risk-based regulatory capital ratios in 2014, as required under the Final Basel III Capital Rules. However, beginning on January 1, 2015, we will use the Basel III Standardized Approach for calculating our risk-weighted assets in our risk-based regulatory capital ratios.

The following table compares our common equity Tier 1 capital and risk-weighted assets as of September 30, 2014, calculated based on the Final Basel III Capital Rules, subject to applicable transition provisions, to our estimated common equity Tier 1 capital and risk-weighted assets as of September 30, 2014, calculated under the Basel III Standardized Approach, as it applies when fully phased-in. Our estimated common equity Tier 1 capital ratio under fully phased-in Basel III Standardized Approach is based on our interpretations, expectations and assumptions of relevant regulations and interpretations provided by our regulators and is subject to change based on changes to future regulations and interpretations.

See the table and notes below for further discussion on our interpretations, expectations and assumptions used in calculating this ratio.

Table 16: Estimated Common Equity Tier 1 Ratio under Fully Phased-In Basel III Standardized Approach⁽¹⁾

(Dollars in millions)	September 30, 2014	
Common equity Tier 1 capital under Basel III Standardized	\$29,116	
Adjustments related to AOCI ⁽²⁾	(412))
Adjustments related to intangibles ⁽²⁾	(1,064))
Other adjustments ⁽²⁾	(1))
Estimated common equity Tier 1 capital under fully phased-in Basel III Standardized	\$27,639	
Risk-weighted assets under Basel I	\$228,759	
Adjustments for Basel III Standardized ⁽³⁾	5,159	
Estimated risk-weighted assets under Basel III Standardized	\$233,918	
Estimated common equity Tier 1 capital ratio under fully phased-in Basel III Standardized ⁽⁴⁾	11.8	%

Estimated Common Equity Tier 1 Ratio under Fully Phased-In Basel III Standardized Approach is a non-GAAP

⁽¹⁾ financial measure. We believe the ratio is helpful to investors by showing the impact of future regulatory capital standards on our capital ratios.

⁽²⁾ Assumes adjustments are fully phased-in.

Adjustments to the Basel I approach to calculating risk-weighted assets include higher risk weights for exposures 90 days or more past due or in nonaccrual, high volatility commercial real estate, securitization exposures and corresponding adjustments to PCCR intangibles, deferred tax assets and certain other assets in the calculation of common equity Tier 1 capital under the Basel III Standardized Approach.

⁽⁴⁾ Calculated by dividing estimated common equity Tier 1 capital under the fully phased-in Basel III Standardized Approach by estimated risk-weighted assets under the Basel III Standardized Approach.

Under the Final Basel III Capital Rules, when we complete our parallel run for the Advanced Approaches, our minimum risk-based capital requirement will be the greater requirement of the Basel III Standardized Approach and the Basel III Advanced Approaches. See “Supervision and Regulation—Basel III and U.S. Capital Rules” in our 2013 Annual Report on Form 10-K for additional information. Based on our business mix, we anticipate that we will need to hold more regulatory capital under the Basel III Advanced Approaches than under Basel I or the Basel III

Standardized Approach to meet our minimum required regulatory capital ratios.

Capital Planning and Regulatory Stress Testing

In November 2011, the Federal Reserve finalized capital planning rules applicable to large bank holding companies like us. Under these rules, bank holding companies with consolidated assets of \$50 billion or more must submit a capital plan to the Federal

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Reserve on an annual basis that contains a description of all planned capital actions, including dividends or stock repurchases, over a nine-quarter planning horizon beginning with the fourth quarter of the calendar year prior to the submission of the capital plan (“CCAR cycle”). The bank holding company may take the capital actions in its capital plan if the Federal Reserve provides a non-objection to the plan. The Federal Reserve’s objection or non-objection applies specifically to capital actions during the four quarters beginning with the second quarter of the second calendar year in the planning horizon. The purpose of the rules is to ensure that large bank holding companies have robust, forward-looking capital planning processes that account for their unique risks and capital needs to continue operations through times of economic and financial stress. On October 17, 2014, the Federal Reserve issued a final rule to modify the regulations for capital planning and stress testing. For additional information, see “Part I—Item 2—Management Discussion and Analysis of Financial Condition and Results of Operations—Supervision and Regulation.”

As a result of the Federal Reserve’s non-objection to our 2014 capital plan, we expect to maintain our quarterly dividend of \$0.30 per share, subject to approval by our Board of Directors. In addition, our Board of Directors has authorized the repurchase of up to \$2.5 billion of shares of common stock through the end of the first quarter of 2015.

Equity Offerings and Transactions

On October 31, 2014, the Company issued and sold 20,000,000 depositary shares (“Depositary Shares”), each representing a 1/40th interest in a share of Fixed Rate Non-Cumulative Perpetual Preferred Stock, Series D, \$0.01 par value, with a liquidation preference of \$25 per Depositary Share (equivalent to \$1,000 per share of Series D Preferred Stock) (the “Series D Preferred Stock”). Dividends will accrue on the Series D Preferred Stock at a rate of 6.70% per annum, payable quarterly in arrears. The net proceeds of the offering of the 20,000,000 Depositary Shares were approximately \$484 million, after deducting underwriting commissions and offering expenses. Under the terms of the Series D Preferred Stock, the ability of the Company to pay dividends on, make distributions with respect to, or to repurchase, redeem or acquire its common stock or any preferred stock ranking on parity with or junior to the Series D Preferred Stock, is subject to restrictions in the event that the Company does not declare and either pay or set aside a sum sufficient for payment of dividends on the Series D Preferred Stock for the immediately preceding dividend period.

Dividend Policy and Stock Purchases

We paid common stock dividends of \$0.30 per share in the third quarter of 2014. During the third quarter, we also paid preferred stock dividends of \$15.00 per share on the outstanding shares of our 6.00% fixed-rate non-cumulative perpetual preferred stock, Series B (“Series B Preferred Stock”) and \$13.7153 per share on the outstanding shares of our 6.25% fixed-rate non-cumulative perpetual preferred stock Series C (“Series C Preferred Stock”).

On October 30, 2014, our Board of Directors declared a quarterly dividend of \$0.30 per share, payable November 20, 2014 and quarterly dividends on our Series B Preferred Stock and Series C Preferred Stock payable on December 1, 2014. Based on these declarations, the Company will pay approximately \$167 million in common equity dividends and approximately \$21 million in total preferred dividends in the fourth quarter of 2014.

The declaration and payment of dividends to our stockholders, as well as the amount thereof, are subject to the discretion of our Board of Directors and depend upon our results of operations, financial condition, capital levels, cash requirements, future prospects and other factors deemed relevant by the Board of Directors. As a bank holding company, our ability to pay dividends is largely dependent upon the receipt of dividends or other payments from our subsidiaries. Regulatory restrictions exist that limit the ability of the Banks to transfer funds to our bank holding company. Funds available for dividend payments from COBNA and CONA were \$1.6 billion and \$138 million, respectively, as of September 30, 2014. There can be no assurance that we will declare and pay any dividends. For additional information on dividends, see “Part I—Item 1. Business—Supervision and Regulation—Dividends, Stock Purchases and Transfer of Funds” in our 2013 Form 10-K.

As disclosed in “Capital Planning and Regulatory Stress Testing” above, we plan to repurchase up to \$2.5 billion of common stock by the end of the first quarter of 2015, through the 2014 Share Repurchase Program approved by our Board of Directors. Through the end of the third quarter of 2014, we have repurchased approximately \$1.5 billion of shares as a part of this program.

The timing and exact amount of any common stock repurchases will depend on various factors, including market conditions, our capital position and amount of retained earnings. Our share repurchase program does not include specific price targets, may be executed through open market purchases or privately negotiated transactions, including utilizing Rule 10b5-1 programs, and may be suspended at any time. For additional information on stock repurchases, see “Part I—Item 1. Business—Supervision and Regulation—Dividends, Stock Repurchases and Transfer of Funds” in our 2013 Form 10-K.

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RISK MANAGEMENT

Overview

We use a risk framework to manage risk. We execute against our risk management framework with the “Three Lines of Defense” risk management model to demonstrate and structure the roles, responsibilities and accountabilities in the organization for taking and managing risk. The “First Line of Defense” is comprised of the business areas that through their day-to-day business activities take risk on our behalf. As the business owner, the first line is responsible for identifying, assessing, managing and controlling that risk, and for mitigating our overall risk exposure. The “Second Line of Defense” provides oversight of first line risk taking and management, and is primarily comprised of our Risk Management organization. The second line assists in determining risk capacity, risk appetite, and the strategies, policies and structure for managing risks. The second line is both an “expert advisor” to the first line and an “effective challenger” of first line risk activities. The “Third Line of Defense” is comprised of our internal audit and credit review functions. The third line provides independent and objective assurance to senior management and to the Board of Directors that first and second line risk management and internal control systems and governance processes are well-designed and working as intended. Our risk framework, which is built around governance, processes and people, consists of the following eight key elements:

- Establish governance processes, accountabilities, and risk appetites
- Identify and assess risks and ownership
- Develop and operate controls, monitoring and mitigation plans
- Test and detect control gaps and perform corrective action
- Escalate key risks and gaps to executive management, and when appropriate the Board of Directors
- Calculate and allocate capital in alignment with risk management and measurement processes (including stress testing)
- Support with the right culture, talent and skills
- Enable with right data, infrastructure and programs

We provide additional discussion of our risk management principles, roles and responsibilities, framework and risk appetite under “MD&A—Risk Management” in our 2013 Form 10-K.

CREDIT RISK PROFILE

Our loan portfolio accounts for the substantial majority of our credit risk exposure. Our lending activities are governed under our credit policy and are subject to independent review and approval. Below we provide information about the composition of our loan portfolio, key concentrations and credit performance metrics.

We also engage in certain non-lending activities that may give rise to credit and counterparty settlement risk, including the purchase of securities for our investment securities portfolio, entering into derivative transactions to manage our market risk exposure and to accommodate customers, foreign exchange transactions, and customer overdrafts. We provide additional information on credit risk related to our investment securities portfolio under “Consolidated Balance Sheets Analysis—Investment Securities” and credit risk related to derivative transactions in “Note 9—Derivative Instruments and Hedging Activities.”

Loan Portfolio Composition

We provide a variety of lending products. Our primary products include credit cards, auto loans, home loans and commercial loans. For information on our lending policies and procedures, including our underwriting criteria for our primary loan products, see “MD&A—Credit Risk Profile” in our 2013 Form 10-K.

Our loan portfolio consists of loans held for investment, including restricted loans underlying our consolidated securitization trusts, and loans held for sale. Table 17 presents the composition of our portfolio of loans held for investment, by portfolio segment, as of September 30, 2014 and December 31, 2013. Table 17 and the credit metrics presented in this section exclude loans held for

sale, which are carried at lower of cost or fair value and totaled \$427 million and \$218 million as of September 30, 2014, and December 31, 2013, respectively.

Table 17: Loan Portfolio Composition

(Dollars in millions)	September 30, 2014				December 31, 2013			
	Loans	Acquired Loans	Total	% of Total	Loans	Acquired Loans	Total	% of Total
Credit Card:								
Domestic credit card ⁽¹⁾	\$73,115	\$28	\$73,143	36.3 %	\$73,192	\$63	\$73,255	37.1 %
International credit card	7,488	—	7,488	3.7	8,050	—	8,050	4.1
Total credit card	80,603	28	80,631	40.0	81,242	63	81,305	41.2
Consumer Banking:								
Auto	36,253	1	36,254	18.0	31,852	5	31,857	16.2
Home loan	6,804	24,399	31,203	15.4	7,098	28,184	35,282	17.9
Retail banking	3,557	47	3,604	1.8	3,587	36	3,623	1.8
Total consumer banking	46,614	24,447	71,061	35.2	42,537	28,225	70,762	35.9
Commercial Banking:⁽²⁾								
Commercial and multifamily real estate	22,832	63	22,895	11.4	20,666	84	20,750	10.5
Commercial and industrial	25,924	147	26,071	12.9	23,131	178	23,309	11.8
Total commercial lending	48,756	210	48,966	24.3	43,797	262	44,059	22.3
Small-ticket commercial real estate	822	—	822	0.4	952	—	952	0.5
Total commercial banking	49,578	210	49,788	24.7	44,749	262	45,011	22.8
Other:								
Other loans	112	—	112	0.1	121	—	121	0.1
Total loans held for investment	\$176,907	\$24,685	\$201,592	100.0 %	\$168,649	\$28,550	\$197,199	100.0 %

(1) Includes installment loans of \$171 million and \$323 million as of September 30, 2014 and December 31, 2013, respectively.

(2) Includes construction loans and land development loans totaling \$2.2 billion and \$2.0 billion as of September 30, 2014 and December 31, 2013, respectively.

Acquired Loans

The substantial majority of our home loan portfolio was acquired in the ING Direct and CCB acquisitions, which were recorded at fair value at acquisition and subsequently accounted for based on expected cash flows to be collected. The difference between the fair value at acquisition and expected cash flows represents the accretable yield, which is recognized in interest income over the life of the loans. The difference between the contractual payments on the loans and expected cash flows represents the nonaccretable difference or the amount of principal and interest not considered collectible, which incorporates future expected credit losses over the life of the loans. Decreases in expected cash flows resulting from further credit deterioration from the previous estimate, will generally result in an impairment charge recognized in our provision for credit losses and an increase in the allowance for loan and lease losses. The expected cash flows for our acquired home loan portfolio are significantly impacted by future expectations of home prices and interest rates. Decreases in expected cash flows that result from declining conditions, particularly associated with these variables, could result in an increase in the allowance for loan and lease losses and reduction in accretable yield.

Charge-offs are not recorded until the expected credit losses within the nonaccretable difference is depleted. In addition, Acquired Loans are not initially classified as delinquent or nonperforming as we expect to collect our net investment in these loans and the nonaccretable difference is expected to absorb the majority of the losses associated with these loans. The period-end carrying value of Acquired Loans in our home loan portfolio was \$24.4 billion and \$28.2 billion as of September 30, 2014 and December 31, 2013, respectively.

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Table 18 presents the relative size of Acquired Loans in our home loan portfolio, by lien priority.

Table 18: Home Loan: Risk Profile by Lien Priority

		September 30, 2014					
		Loans		Acquired Loans		Total Home Loans	
(Dollars in millions)		Amount	% of Total	Amount	% of Total	Amount	% of Total
Lien type:							
1st lien		\$5,762	18.5 %	\$24,026	77.0 %	\$29,788	95.5 %
2nd lien		1,042	3.3	373	1.2	1,415	4.5
Total		\$6,804	21.8 %	\$24,399	78.2 %	\$31,203	100.0 %
		December 31, 2013					
		Loans		Acquired Loans		Total Home Loans	
(Dollars in millions)		Amount	% of Total	Amount	% of Total	Amount	% of Total
Lien type:							
1st lien		\$6,020	17.1 %	\$27,768	78.7 %	\$33,788	95.8 %
2nd lien		1,078	3.0	416	1.2	1,494	4.2
Total		\$7,098	20.1 %	\$28,184	79.9 %	\$35,282	100.0 %

See “Note 4—Loans” in this Report for additional credit quality information. See “Note 1—Summary of Significant Accounting Policies” in our 2013 Form 10-K for information on our accounting policies for Acquired Loans, delinquent loans, nonperforming loans, net charge-offs and troubled debt restructurings (“TDRs”) for each of our loan categories.

Credit Risk Measurement

We closely monitor economic conditions and loan performance trends to assess and manage our exposure to credit risk. Key metrics we track in evaluating the credit quality of our loan portfolio include delinquency and nonperforming asset rates, as well as net charge-off rates and our internal risk ratings of larger balance commercial loans. Trends in delinquency rates are a primary indicator of credit risk within our consumer loan portfolios, as changes in delinquency rates provide an early warning of changes in credit losses. The primary indicator of credit risk in our commercial loan portfolios is our internal risk ratings. Because we generally classify loans that have been delinquent for an extended period of time and other loans with significant risk of loss as nonperforming, the level of nonperforming assets represents another indicator of the potential for future credit losses. In addition to delinquency rates, the geographic distribution of our loans provides insight as to the credit quality of the portfolio based on regional economic conditions.

We underwrite most consumer loans using proprietary models, which are typically based on credit bureau data, including borrower credit scores, along with application information and, where applicable, collateral, and deal structure data. We continuously adjust our management of credit lines and collection strategies based on customer behavior and risk profile changes. We use borrower credit scores for subprime classification, for competitive benchmarking, and in some cases to drive product segmentation decisions.

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The following table provides details on the credit scores of our domestic credit card and auto loan portfolios.

Table 19: Credit Score Distribution

(Percentage of portfolio with estimated credit scores)	September 30, 2014	December 31, 2013	December 31, 2012	
Domestic credit card - Refreshed FICO scores: ⁽¹⁾				
Greater than 660	68	% 69	% 69	%
660 or below	32	31	31	
Total	100	% 100	% 100	%
Auto - At origination FICO scores: ⁽²⁾				
Greater than 660	46	% 42	% 35	%
621 - 660	16	17	18	
620 or below	38	41	47	
Total	100	% 100	% 100	%

Credit scores generally represent FICO scores. These scores are obtained from one of the major credit bureaus at
(1) origination and are refreshed monthly thereafter. We approximate non-FICO credit scores to comparable FICO scores for consistency. Balances for which no credit score is available or the credit score is invalid are included in the 660 or below category.

Credit scores represent FICO scores. These scores are obtained from three credit bureaus at the time of
(2) application and are not refreshed thereafter. The reported FICO score distribution in the table above is based on the average scores. Balances for which no credit score is available or the credit score is invalid are included in the 620 or below category.

We present information in the section below on the credit performance of our loan portfolio, including the key metrics we use in tracking changes in the credit quality of our loan portfolio. We also present adjusted credit quality metrics excluding the impact from Acquired Loans.

See “Note 4—Loans” in this Report for additional credit quality information. See “Note 1—Summary of Significant Accounting Policies” in our 2013 Form 10-K for information on our accounting policies for delinquent, nonperforming loans, net charge-offs and TDRs for each of our loan categories.

Delinquency Rates

We consider the entire balance of an account to be delinquent if the minimum required payment is not received by the customer’s due date, measured at the reporting date. Our 30+ day delinquency metrics include all loans held for investment that are 30 or more days past due, whereas our 30+ day performing delinquency metrics include loans that are 30 or more days past due but currently classified as performing and accruing interest. The 30+ day delinquency and 30+ day performing delinquency metrics are generally the same for credit card loans, as we continue to classify the substantial majority of credit card loans as performing until the account is charged-off, typically when the account is 180 days past due. See “Note 1—Summary of Significant Accounting Policies” in our 2013 Form 10-K for information on our policies for classifying loans as nonperforming for each of our loan categories.

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Table 20 presents our 30+ day performing and total 30+ day delinquency rates, by portfolio segment, as of September 30, 2014 and December 31, 2013. It also presents the adjusted rates, which exclude Acquired Loans from the denominator as they are accounted for based on cash flows expected to be collected over the life of the loans.

Table 20: 30+ Day Delinquencies

(Dollars in millions)	September 30, 2014				December 31, 2013			
	30+ Day Performing		30+ Day Total		30+ Day Performing		30+ Day Total	
	Amount	Rate ⁽¹⁾	Amount	Rate ⁽¹⁾	Amount	Rate ⁽¹⁾	Amount	Rate ⁽¹⁾
Credit Card:								
Domestic credit card	\$2,347	3.21 %	\$2,347	3.21 %	\$2,514	3.43 %	\$2,514	3.43 %
International credit card	250	3.34	306	4.08	299	3.71	367	4.56
Total credit card	2,597	3.22	2,653	3.29	2,813	3.46	2,881	3.54
Consumer Banking:								
Auto	2,227	6.14	2,404	6.63	2,181	6.85	2,375	7.46
Home loan ⁽²⁾	45	0.14	277	0.89	55	0.16	323	0.91
Retail banking	19	0.53	31	0.85	25	0.69	52	1.44
Total consumer banking	2,291	3.22	2,712	3.82	2,261	3.20	2,750	3.89
Commercial Banking:								
Commercial and multifamily real estate	28	0.12	63	0.27	29	0.14	64	0.31
Commercial and industrial	38	0.15	106	0.41	73	0.31	108	0.46
Total commercial lending	66	0.14	169	0.34	102	0.23	172	0.39
Small-ticket commercial real estate	5	0.55	8	0.92	8	0.79	11	1.17
Total commercial banking	71	0.14	177	0.35	110	0.24	183	0.41
Other:								
Other loans	3	3.64	14	12.88	4	3.32	19	15.72
Total	\$4,962	2.46	\$5,556	2.76	\$5,188	2.63	\$5,833	2.96

(1) Calculated by loan category by dividing 30+ day delinquent loans as of the end of the period by period-end loans held for investment for the specified loan category, including Acquired Loans as applicable.

(2) Excluding the impact of Acquired Loans, the 30+ day performing and total 30+ day delinquency rates for home loan portfolio are 0.65% and 4.07%, respectively, as of September 30, 2014, and 0.78% and 4.55%, respectively, as of December 31, 2013.

Table 21 presents an aging of 30+ day delinquent loans included in the above table.

Table 21: Aging and Geography of 30+ Day Delinquent Loans

(Dollars in millions)	September 30, 2014			December 31, 2013		
	Amount	% of Total Loans ⁽¹⁾		Amount	% of Total Loans ⁽¹⁾	
Total loan portfolio	\$201,592	100.0 %		\$197,199	100.00 %	
Delinquency status:						
30 – 59 days	\$2,582	1.28		\$2,617	1.33	
60 – 89 days	1,337	0.67		1,344	0.68	
90 + days	1,637	0.81		1,872	0.95	
Total	\$5,556	2.76 %		\$5,833	2.96 %	
Geographic region:						
Domestic	\$5,250	2.61 %		\$5,466	2.77 %	
International	306	0.15		367	0.19	
Total	\$5,556	2.76 %		\$5,833	2.96 %	

(1) Calculated by dividing loans in each delinquency status category or geographic region as of the end of the period by the total loans held for investment, including Acquired Loans accounted for based on expected cash flows.

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Table 22 summarizes loans that were 90 days or more past due as to interest or principal and still accruing interest as of September 30, 2014 and December 31, 2013. These loans consist primarily of credit card accounts between 90 days and 179 days past due. As permitted by regulatory guidance issued by the Federal Financial Institutions Examination Council (“FFIEC”), we generally continue to accrue interest and fees on domestic credit card loans through the date of charge-off, which is typically in the period the account becomes 180 days past due. While domestic credit card loans typically remain on accrual status until the loan is charged-off, we reduce the balance of our credit card receivables by the amount of finance charges and fees billed but not expected to be collected and exclude this amount from revenue.

Table 22: 90+ Day Delinquent Loans Accruing Interest

(Dollars in millions)	September 30, 2014		December 31, 2013	
	Amount	% of Total Loans ⁽¹⁾	Amount	% of Total Loans ⁽¹⁾
Loan category:				
Credit card	\$1,109	1.38 %	\$1,283	1.58 %
Consumer banking	1	0.00	2	0.00
Commercial banking	6	0.01	6	0.01
Total	\$1,116	0.55	\$1,291	0.65
Geographic region:				
Domestic	\$1,040	0.54	\$1,195	0.63
International	76	1.01	96	1.19
Total	\$1,116	0.55	\$1,291	0.65

⁽¹⁾ Delinquency rates are calculated for each loan category by dividing 90+ day delinquent loans accruing interest by period-end loans held for investment for the specified loan category.

Nonperforming Loans and Nonperforming Assets

Nonperforming assets consist of nonperforming loans, foreclosed property and repossessed assets and the net realizable value of auto loans that have been charged-off as a result of a bankruptcy. Nonperforming loans generally include loans that have been placed on nonaccrual status and certain restructured loans whose contractual terms have been modified in a manner that grants a concession to a borrower experiencing financial difficulty. In addition, we separately track and report Acquired Loans accounted for based on expected cash flows and disclose our delinquency and nonperforming loan rates with and without these Acquired Loans. See “Note 1—Summary of Significant Accounting Policies” in our 2013 Form 10-K for information on our policies for classifying loans as nonperforming for each of our loan categories.

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Table 23 presents comparative information on nonperforming loans, by portfolio segment, and other nonperforming assets, as of September 30, 2014 and December 31, 2013. We do not classify loans held for sale as nonperforming, as they are recorded at the lower of cost or fair value.

Table 23: Nonperforming Loans and Other Nonperforming Assets⁽¹⁾

(Dollars in millions)	September 30, 2014		December 31, 2013		
	Amount	% of Total Loans HFI	Amount	% of Total Loans HFI	
Nonperforming loans held for investment:					
Credit Card:					
International credit card	\$74	0.98	% \$88	1.10	%
Total credit card	74	0.09	88	0.11	
Consumer Banking:					
Auto	177	0.49	194	0.61	
Home loan ⁽²⁾	325	1.04	376	1.06	
Retail banking	19	0.54	41	1.13	
Total consumer banking ⁽²⁾	521	0.73	611	0.86	
Commercial Banking:					
Commercial and multifamily real estate	60	0.26	52	0.25	
Commercial and industrial	97	0.37	93	0.40	
Total commercial lending	157	0.32	145	0.33	
Small-ticket commercial real estate	4	0.42	4	0.41	
Total commercial banking	161	0.32	149	0.33	
Other:					
Other loans	16	14.66	19	15.83	
Total nonperforming loans held for investment ⁽²⁾⁽³⁾	\$772	0.38	\$867	0.44	
Other nonperforming assets ⁽⁴⁾ :					
Foreclosed property ⁽⁵⁾	\$129	0.06	\$113	0.06	
Other assets ⁽⁶⁾	167	0.08	160	0.08	
Total other nonperforming assets	296	0.15	273	0.14	
Total nonperforming assets ⁽⁷⁾	\$1,068	0.53	\$1,140	0.58	

We recognized interest income for loans classified as nonperforming of \$22 million and \$27 million in the first nine months of 2014 and 2013, respectively. Interest income foregone related to nonperforming loans was \$33

⁽¹⁾ million and \$44 million in the first nine months of 2014 and 2013, respectively. Foregone interest income represents the amount of interest income that would have been recorded during the period for nonperforming loans as of the end of the period had the loans performed according to their contractual terms.

The nonperforming loan ratio, excluding Acquired Loans' impact for our home loan portfolio, total consumer ⁽²⁾ banking, and total nonperforming loans held for investment was 4.77%, 1.12%, and 0.44%, respectively, as of September 30, 2014, compared with 5.29%, 1.44%, and 0.51%, respectively, as of December 31, 2013.

⁽³⁾ Nonperforming loans as a percentage of total loans held for investment, excluding the impact of domestic credit card loans, was 0.60% and 0.70% as of September 30, 2014 and December 31, 2013, respectively.

⁽⁴⁾ The denominator used in calculating the nonperforming asset ratios consists of total loans held for investment and other nonperforming assets.

⁽⁵⁾ Includes foreclosed properties related to Acquired Loans of \$84 million and \$68 million as of September 30, 2014 and December 31, 2013, respectively.

⁽⁶⁾ Includes the net realizable value of auto loans that have been charged-off as a result of a bankruptcy and repossessed assets obtained in satisfaction of auto loans.

⁽⁷⁾

The nonperforming asset ratio, excluding the impact of Acquired Loans was 0.56% and 0.63% as of September 30, 2014 and December 31, 2013, respectively.

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Net Charge-Offs

Net charge-offs consist of the unpaid principal balance of loans held for investment that we determine are uncollectible, net of recovered amounts. We exclude accrued and unpaid finance charges and fees and fraud losses from charge-offs. Net charge-offs are recorded as a reduction to the allowance for loan and lease losses and subsequent recoveries of previously charged-off amounts are credited to the allowance for loan and lease losses. Costs incurred to recover charged-off loans are recorded as collection expenses and included on our consolidated statements of income as a component of other non-interest expense. Our charge-off policy for loans varies based on the loan type. See “Note 1—Summary of Significant Accounting Policies—Loans” in our 2013 Form 10-K for information on our charge-off policy for each of our loan categories.

Table 24 presents our net charge-off amounts and rates, by portfolio segment, in the third quarter and first nine months of 2014 and 2013.

Table 24: Net Charge-Offs

(Dollars in millions)	Three Months Ended September 30,					
	2014			2013		
	Amount	Rate ⁽¹⁾	Adjusted Rate ⁽²⁾	Amount	Rate ⁽¹⁾	Adjusted Rate ⁽²⁾
Credit Card:						
Domestic credit card	\$508	2.83 %	2.83 %	\$642	3.67 %	3.68 %
International credit card	64	3.32	3.32	92	4.71	4.71
Total credit card	572	2.88	2.88	734	3.78	3.78
Consumer Banking:						
Auto	176	1.98	1.98	152	2.01	2.01
Home loan	2	0.02	0.11	5	0.06	0.30
Retail banking	12	1.36	1.38	13	1.38	1.40
Total consumer banking	190	1.07	1.65	170	0.95	1.64
Commercial Banking:						
Commercial and multifamily real estate	(5)	(0.10)	(0.10)	(5)	(0.11)	(0.11)
Commercial and industrial	(1)	(0.01)	(0.01)	9	0.18	0.18
Total commercial lending	(6)	(0.05)	(0.05)	4	0.04	0.04
Small-ticket commercial real estate	0	(0.01)	(0.01)	4	1.26	1.26
Total commercial banking	(6)	(0.05)	(0.05)	8	0.07	0.07
Other:						
Other loans	0	(0.61)	(0.61)	5	12.17	15.40
Total net charge-offs	\$756	1.52	1.73	\$917	1.92	2.29
Average loans held for investment	\$199,422			\$191,135		
Average loans held for investment (excluding Acquired Loans)	174,318			160,422		

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(Dollars in millions)	Nine Months Ended September 30,					
	2014			2013		
	Amount	Rate ⁽¹⁾	Adjusted Rate ⁽²⁾	Amount	Rate ⁽¹⁾	Adjusted Rate ⁽²⁾
Credit Card:						
Domestic credit card	\$1,818	3.45 %	3.45 %	\$2,218	4.14 %	4.14 %
International credit card	219	3.81	3.81	288	4.79	4.79
Total credit card	2,037	3.48	3.48	2,506	4.20	4.21
Consumer Banking:						
Auto	421	1.65	1.65	366	1.69	1.69
Home loan	12	0.05	0.22	13	0.04	0.23
Retail banking	27	1.00	1.01	44	1.58	1.60
Total consumer banking	460	0.87	1.37	423	0.77	1.40
Commercial Banking:						
Commercial and multifamily real estate	(5)	(0.03)	(0.03)	(3)	(0.02)	(0.02)
Commercial and industrial	3	0.02	0.02	13	0.08	0.09
Total commercial lending	(2)	0.00	0.00	10	0.04	0.04
Small-ticket commercial real estate	3	0.44	0.44	9	1.04	1.04
Total commercial banking	1	0.00	0.00	19	0.06	0.06
Other:						
Other loans	1	0.33	0.33	17	13.31	16.69
Total net charge-offs	\$2,499	1.70	1.96	\$2,965	2.05	2.48
Average loans held for investment	\$196,068			\$192,547		
Average loans held for investment (excluding Acquired Loans)	169,616			159,359		

(1) Calculated for each loan category by dividing annualized net charge-offs for the period by average loans held for investment during the period.

(2) Calculated by excluding Acquired Loans from the denominator.

For information regarding management's expectations of net charge-offs, see "MD&A—Business Segment Expectations".

Loan Modifications and Restructurings

As part of our loss mitigation efforts, we may provide short-term (three to twelve months) or long-term (greater than twelve months) modifications to a borrower experiencing financial difficulty to improve long-term collectability of the loan and to avoid the need for foreclosure or repossession of collateral.

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Table 25 presents our loans modified in TDRs as of September 30, 2014 and December 31, 2013. It excludes loan modifications that do not meet the definition of a TDR and Acquired Loans accounted for based on expected cash flows, which we track and report separately.

Table 25: Loan Modifications and Restructurings

(Dollars in millions)	September 30, 2014			December 31, 2013		
	Amount	% of Total Modifications		Amount	% of Total Modifications	
Modified and restructured loans:						
Credit card ⁽¹⁾	\$706	43.8	%	\$780	46.4	%
Auto	399	24.8		355	21.1	
Home loan	220	13.6		244	14.5	
Retail banking	39	2.4		64	3.8	
Commercial banking	249	15.4		238	14.2	
Total	\$1,613	100.0	%	\$1,681	100.0	%
Status of modified and restructured loans:						
Performing	\$1,199	74.3	%	\$1,250	74.4	%
Nonperforming	414	25.7		431	25.6	
Total	\$1,613	100.0	%	\$1,681	100.0	%

(1) Amount reported reflects the total outstanding customer balance, which consists of unpaid principal balance, accrued interest and fees.

The majority of our credit card TDRs involve reducing the interest rate on the account and placing the customer on a fixed payment plan not exceeding 60 months. We determine the effective interest rate for purposes of measuring impairment on modified loans that involve a reduction and are considered to be a TDR based on the interest rate in effect immediately prior to the loan entering the modification program. In some cases, the interest rate on a credit card account is automatically increased due to non-payment, late payment or similar events. In all cases, we cancel the customer's available line of credit on the credit card. If the customer does not comply with the modified payment terms, then the credit card loan agreement may revert to its original payment terms, with the amount of any loan outstanding reflected in the appropriate delinquency category. The loan amount may then be charged-off in accordance with our standard charge-off policy.

Within the Consumer Banking business, the majority of our modified loans receive an extension, while a portion receive an interest rate reduction or principal reduction. Their impairment is determined using the present value of expected cash flows, or a collateral evaluation for auto and home loans that were charged down to fair value. In the Commercial Banking business, the majority of modified loans receive an extension, with a portion of these loans receiving an interest rate reduction. The impairment on modified commercial loans is generally determined based on the underlying collateral value. We provide additional information on modified loans accounted for as TDRs, including the performance of those loans subsequent to modification, in "Note 4—Loans."

Impaired Loans

A loan is considered impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due from the borrower in accordance with the original contractual terms of the loan. Generally, we report loans as impaired based on the method for measuring impairment in accordance with applicable accounting guidance. Loans defined as individually impaired include larger balance commercial nonperforming loans and TDRs. Loans held for sale are not reported as impaired, as these loans are recorded at lower of cost or fair value. Impaired loans also exclude Acquired Loans accounted for based on expected cash flows because this accounting methodology takes into consideration future credit losses expected to be incurred, as discussed above under "Summary of Selected Financial Data."

Impaired loans, including TDRs, totaled \$1.9 billion as of both September 30, 2014 and December 31, 2013. TDRs accounted for \$1.6 billion and \$1.7 billion of impaired loans as of September 30, 2014 and December 31, 2013,

respectively. We provide additional information on our impaired loans, including the allowance for loan and lease losses established for these loans, in “Note 4—Loans” and “Note 5—Allowance for Loan and Lease Losses.”

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Allowance for Loan and Lease Losses

Our allowance for loan and lease losses represents management's best estimate of incurred loan and lease credit losses inherent in our held for investment portfolio as of each balance sheet date. The allowance for loan and lease losses is increased through the provision for credit losses and reduced by net charge-offs. We provide additional information on the methodologies and key assumptions used in determining our allowance for loan and lease losses in "Note 1—Summary of Significant Accounting Policies" in our 2013 Form 10-K.

Our allowance for loan and lease losses decreased by \$103 million from \$4.3 billion as of December 31, 2013 and increased by \$214 million, from \$4.0 billion as of June 30, 2014, to \$4.2 billion as of September 30, 2014. The allowance coverage ratio declined to 2.09% as of September 30, 2014, from 2.19% as of December 31, 2013. The release in allowance for loan and lease losses in the first and second quarters of 2014 was mainly due to credit improvements, partially offset by a build in the third quarter of 2014 driven by loan growth and higher delinquency inventories increasing our loss expectations.

Table 26 presents changes in our allowance for loan and lease losses for the third quarter and first nine months of 2014 and 2013, and details the provision for credit losses recognized on our consolidated statements of income, and charge-offs and recoveries by portfolio segment.

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Table 26: Allowance for Loan and Lease Losses Activity

(Dollars in millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Balance at beginning of period, as reported	\$3,998	\$4,407	\$4,315	\$5,156
Provision for credit losses ⁽¹⁾	988	829	2,412	2,442
Charge-offs:				
Credit Card:				
Domestic credit card	(768)	(895)	(2,599)	(3,047)
International credit card	(117)	(141)	(376)	(432)
Total credit card	(885)	(1,036)	(2,975)	(3,479)
Consumer Banking:				
Auto	(245)	(210)	(633)	(545)
Home loan	(4)	(6)	(23)	(18)
Retail banking	(15)	(18)	(44)	(62)
Total consumer banking	(264)	(234)	(700)	(625)
Commercial Banking:				
Commercial and multifamily real estate	(1)	(1)	(3)	(5)
Commercial and industrial	(1)	(12)	(11)	(22)
Total commercial lending	(2)	(13)	(14)	(27)
Small-ticket commercial real estate	(2)	(4)	(5)	(16)
Total commercial banking	(4)	(17)	(19)	(43)
Other loans	(2)	(7)	(8)	(22)
Total charge-offs	(1,155)	(1,294)	(3,702)	(4,169)
Recoveries:				
Credit Card:				
Domestic credit card	260	253	781	829
International credit card	53	49	157	144
Total credit card	313	302	938	973
Consumer Banking:				
Auto	69	58	212	179
Home loan	2	1	11	5
Retail banking	3	5	17	18
Total consumer banking	74	64	240	202
Commercial Banking:				
Commercial and multifamily real estate	6	6	8	8
Commercial and industrial	2	3	8	9
Total commercial lending	8	9	16	17
Small-ticket commercial real estate	2	—	2	7
Total commercial banking	10	9	18	24
Other:				
Other loans	2	2	7	5
Total recoveries	399	377	1,203	1,204
Net charge-offs	(756)	(917)	(2,499)	(2,965)
Other changes ⁽²⁾	(18)	14	(16)	(300)
Balance at end of period	\$4,212	\$4,333	\$4,212	\$4,333
			2.09 %	2.26 %

Allowance for loan and lease losses as a percentage of loans held for investment

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The total provision for credit losses reported on our consolidated statements of income consists of a provision for loan and lease losses and a provision for unfunded lending commitments. The table above only presents the (1) provision for loan and lease losses, and does not include the provision for unfunded lending commitments of \$5 million and \$20 million in the third quarter and first nine months of 2014, respectively, and a provision of \$20 million and \$54 million in the third quarter and first nine months of 2013, respectively.

Primarily represents foreign currency translation adjustments and the net impact of loan transfers and sales. In the (2) first quarter of 2013, the allowance for loan and lease losses was reduced by \$289 million attributable to the transfer of the Best Buy loan portfolio from HFI to HFS, which was subsequently sold in the third quarter of 2013. Table 27 presents an allocation of our allowance for loan and lease losses by portfolio segment as of September 30, 2014 and December 31, 2013.

Table 27: Allocation of the Allowance for Loan and Lease Losses

(Dollars in millions)	September 30, 2014			December 31, 2013		
	Amount	% of Total Loans HFI	%	Amount	% of Total Loans HFI	%
Credit Card:						
Domestic credit card	\$2,746	3.75	%	\$2,836	3.87	%
International credit card	311	4.15		378	4.70	
Total credit card	3,057	3.79		3,214	3.95	
Consumer Banking:						
Auto	660	1.82		606	1.90	
Home loan ⁽¹⁾	55	0.18		83	0.24	
Retail banking	57	1.57		63	1.74	
Total consumer banking ⁽¹⁾	772	1.09		752	1.06	
Commercial Banking:						
Commercial and multifamily real estate	151	0.66		143	0.69	
Commercial and industrial	214	0.82		166	0.71	
Total commercial lending	365	0.75		309	0.70	
Small-ticket commercial real estate	13	1.52		29	3.05	
Total commercial banking	378	0.76		338	0.75	
Other:						
Other loans	5	5.00		11	9.09	
Total allowance for loan and lease losses	\$4,212	2.09		\$4,315	2.19	
Total allowance coverage ratios:						
Period-end loans held for investment	\$201,592	2.09		\$197,199	2.19	
Period-end loans held for investment (excluding Acquired Loans)	176,907	2.37		168,649	2.54	
Nonperforming loans ⁽²⁾	772	545.63		867	497.69	
Allowance coverage ratios by loan category⁽³⁾:						
Credit card (30+ day delinquent loans)	2,653	115.23		2,881	111.56	
Consumer banking (30+ day delinquent loans)	2,712	28.45		2,750	27.35	
Commercial banking (nonperforming loans)	161	234.98		149	226.85	

The coverage ratio for home loans and consumer banking, excluding the Acquired Loans' impact, was 0.48%, and (1) 1.61%, respectively, as of September 30, 2014, compared with 0.64% and 1.68%, respectively, as of December 31, 2013.

The allowance for loan and lease losses as a percentage of nonperforming loans, excluding the allowance for loan (2) and lease losses related to our domestic credit card loans, was 189.93% as of September 30, 2014, and 170.59% as of December 31, 2013.

- (3) Calculated based on the total allowance for loan and lease losses divided by the outstanding balance of loans within the specified loan category.

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LIQUIDITY RISK PROFILE

We have established liquidity guidelines that are intended to ensure we have sufficient asset-based liquidity to withstand the potential impact of deposit attrition or diminished liquidity in the funding markets. Our guidelines include maintaining an adequate liquidity reserve to cover our funding requirements as well as any potential deposit run-off and maintaining diversified funding sources to avoid over-dependence on volatile, less reliable funding markets. Our liquidity reserves consist of readily-marketable or pledgable assets which can be used as a source of liquidity, if needed.

Table 28 below presents the composition of our liquidity reserves as of September 30, 2014 and December 31, 2013.

Table 28: Liquidity Reserves

(Dollars in millions)	September 30, 2014	December 31, 2013
Cash and cash equivalents	\$ 6,148	\$6,291
Investment securities available for sale, at fair value	39,665	41,800
Investment securities held to maturity, at fair value	22,928	19,185
Total investment securities portfolio ⁽¹⁾ ⁽²⁾	62,593	60,985
FHLB borrowing capacity secured by loans	30,456	28,623
Outstanding FHLB advances and letters of credit secured by loans	(10,310)	(8,917)
Outstanding FHLB advances and letters of credit secured by securities	(1,004)	(7,808)
Securities encumbered for Public Funds and others	(10,330)	(9,491)
Total liquidity reserves	\$ 77,553	\$69,683

(1) The weighted average life of our securities was approximately 6.1 years and 6.3 years as of September 30, 2014, and December 31, 2013, respectively.

We pledged securities available for sale with a fair value of \$5.8 billion and \$10.7 billion as of September 30, 2014 and December 31, 2013, respectively. We also pledged securities held to maturity with a carrying value of \$13.7 billion and \$8.2 billion as of September 30, 2014 and December 31, 2013, respectively. As of September 30, 2014, \$7.3 billion of the total pledged securities were used to secure our FHLB borrowing capacity.

Our liquidity reserves increased by \$7.9 billion, or 11%, in the first nine months of 2014, to \$77.6 billion as of September 30, 2014, from \$69.7 billion as of December 31, 2013. This increase was primarily attributable to lower FHLB advances due to seasonality and an increase in the fair value of our investment securities. See “MD&A—Risk Management” in our 2013 Form 10-K for additional information on our management of liquidity risk.

Funding

The Company’s primary source of funding comes from deposits. In addition to deposits, the Company raises funding through the purchase of federal funds, the issuance of brokered deposits, FHLB advances secured by certain portions of our loan and securities portfolios, the issuance of senior and subordinated notes, loan securitization transactions and other various types of borrowings. A key objective in our use of these markets is to ensure we maintain access to a diversified mix of wholesale funding sources.

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Deposits

Our deposits provide a stable and relatively low cost of funds and are our largest source of funding. Table 29 provides a comparison of the composition of our deposits, average balances, interest expense and average deposit rates for the first nine months of 2014 and full year 2013.

Table 29: Deposit Composition and Average Deposit Rates

(Dollars in millions)	Nine Months Ended September 30, 2014					Average Deposit Rate	
	Period End Balance	Average Balance	Interest Expense	% of Average Deposits	%		
Non-interest bearing accounts	\$25,388	\$24,196	N/A	11.8	%	N/A	
Interest-bearing checking accounts ⁽¹⁾	40,045	42,260	\$155	20.5		0.49	%
Saving deposits ⁽²⁾	129,989	129,854	563	63.1		0.58	
Time deposits less than \$100,000	5,555	5,797	57	2.8		1.30	
Total core deposits	200,977	202,107	775	98.2		0.51	
Time deposits of \$100,000 or more	2,412	2,637	41	1.3		2.09	
Foreign time deposits ⁽³⁾	875	1,039	3	0.5		0.33	
Total deposits	\$204,264	\$205,783	\$819	100.0	%	0.53	

(Dollars in millions)	Twelve Months Ended December 31, 2013					Average Deposit Rate	
	Period End Balance	Average Balance	Interest Expense	% of Average Deposits	%		
Non-interest bearing accounts	\$22,643	\$21,345	N/A	10.2	%	N/A	
Interest-bearing checking accounts ⁽¹⁾	43,880	43,823	\$254	21.0		0.58	%
Saving deposits ⁽²⁾	127,667	129,373	714	61.8		0.55	
Time deposits less than \$100,000	6,299	8,955	161	4.3		1.80	
Total core deposits	200,489	203,496	1,129	97.3		0.55	
Time deposits of \$100,000 or more	2,852	3,938	108	1.9		2.74	
Foreign time deposits ⁽³⁾	1,182	1,611	4	0.8		0.25	
Total deposits	\$204,523	\$209,045	\$1,241	100.0	%	0.59	

(1) Includes Negotiable Order of Withdrawal (“NOW”) accounts.

(2) Includes Money Market Deposit Accounts (“MMDA”).

(3) Substantially all of our foreign time deposits are greater than \$100,000 as of both September 30, 2014, and December 31, 2013.

Total deposits decreased by \$259 million during the first nine months of 2014, to \$204.3 billion as of September 30, 2014, from \$204.5 billion as of December 31, 2013. The decrease was primarily driven by the run-off of certain deposits, which was partially offset by the growth in our Consumer Banking and Commercial Banking businesses as a result of our continued focus on deepening deposit relationships with existing customers and our continued marketing strategy to attract new business. Our deposits include brokered deposits, which we obtained through the use of third-party intermediaries. Those brokered deposits are reported in saving deposits and time deposits in the above table and totaled \$4.3 billion and \$6.0 billion as of September 30, 2014 and December 31, 2013, respectively.

FDIC limits the use of brokered deposits to “well-capitalized” insured depository institutions and, with a waiver from the FDIC, to “adequately capitalized” institutions. COBNA and CONA were “well-capitalized,” as defined under the federal banking regulatory guidelines, as of both September 30, 2014 and December 31, 2013, and therefore were permitted to maintain brokered deposits.

Short-Term Borrowings and Long-Term Debt

We access the capital markets to meet our funding needs through the issuance of senior and subordinated notes, loan securitization transactions, and federal funds purchased and securities loaned or sold under agreements to repurchase. We participate in the

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federal funds market regularly to take advantage of attractive offers and to keep a visible presence in the market, which is intended to ensure that we are able to access the federal funds market in a time of need. In addition, we may utilize short-term as well as long-term FHLB advances for our funding needs. FHLB advances are secured by our investment securities, residential home loans, multifamily real estate loans, commercial real estate loans and home equity lines of credit.

Our short-term borrowings include those borrowings with an original contractual maturity of one year or less and do not include the current portion of long-term debt. The short-term borrowings, which consist of federal funds purchased and securities loaned or sold under agreements to repurchase, and short-term FHLB advances, decreased by \$4.1 billion in the first nine months of 2014, from \$16.2 billion as of December 31, 2013, to \$12.1 billion as of September 30, 2014. This decrease reflects \$30.7 billion in payoffs of FHLB advances, partially offset by \$25.3 billion in new advances in the first nine months of 2014.

Our long-term debt, which consists of securitized debt obligations, senior and subordinated notes, and long-term FHLB advances, increased by \$5.7 billion in the first nine months of 2014, from \$24.4 billion as of December 31, 2013, to \$30.1 billion as of September 30, 2014. The increase was primarily attributable to new senior unsecured debt issuances of \$7.8 billion and securitized debt issuances of \$3.0 billion, partially offset by \$2.4 billion and \$2.8 billion of senior unsecured note and securitized debt maturities, respectively.

Table 30 provides the average balances and average interest rate of our short-term borrowings for the third quarter and first nine months of 2014 and 2013. This table also presents the period-end balances, weighted average interest rates and the maximum month-end outstanding amounts of our short-borrowings as of September 30, 2014 and December 31, 2013.

Table 30: Short-Term Borrowings

(Dollars in millions)	Three Months Ended September 30,					
	2014	2013	Average	Average	Average	Average
	Average	Average	Interest	Balance	Interest	Rate
	Balance	Balance	Rate		Rate	
Federal funds purchased and repurchase agreements	\$1,781	\$2,022	0.09 %		0.11 %	
FHLB advances	9,450	10,755	0.22		0.19	
Total short-term borrowings	\$11,231	\$12,777	0.20		0.18	
(Dollars in millions)	Nine Months Ended September 30,					
	2014	2013	Average	Average	Average	Average
	Balance	Balance	Interest	Balance	Interest	Rate
			Rate		Rate	
Federal funds purchased and repurchase agreements	\$1,749	\$1,534	0.08 %		0.11 %	
FHLB advances	8,075	12,385	0.23		0.23	
Total short-term borrowings	\$9,824	\$13,919	0.20		0.22	
(Dollars in millions)	September 30, 2014		December 31, 2013			
	Outstanding	Weighted	Maximum	Outstanding	Weighted	Maximum
	Amount	Average	Month-End	Amount	Average	Month-End
		Interest	Outstanding		Interest	Outstanding
		Rate	Amount		Rate	Amount
Federal funds purchased and repurchase agreements	\$2,330	0.05 %	\$2,330	\$915	0.06 %	\$2,258
FHLB advances	9,800	0.22	12,500	15,300	0.25	16,600
Total short-term borrowings	\$12,130	0.18		\$16,215	0.24	

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Table 31 displays the maturity profile, based on contractual maturities, of our short-term borrowings and long-term debt including securitized debt obligations, senior and subordinated notes and other borrowings as of September 30, 2014, and the outstanding balances as of December 31, 2013.

Table 31: Contractual Maturity Profile of Outstanding Debt

(Dollars in millions)	September 30, 2014						Total	December 31, 2013
	Up to 1 Year	> 1 Year to 2 Years	> 2 Years to 3 Years	> 3 Years to 4 Years	> 4 Years to 5 Years	> 5 Years		
Short-term borrowings:								
Federal funds purchased and securities loaned or sold under agreements to repurchase	\$2,330	\$—	\$—	\$—	\$—	\$—	\$2,330	\$915
FHLB advances	9,800	—	—	—	—	—	9,800	15,300
Total short-term borrowings	\$12,130	—	—	—	—	—	12,130	16,215
Long-term debt:								
Securitized debt obligations	365	3,098	5,832	—	1,138	75	10,508	10,289
Senior and subordinated notes:								
Unsecured senior debt	1,637	1,952	3,631	587	4,070	4,058	15,935	10,464
Unsecured subordinated debt	—	1,087	—	—	314	1,198	2,599	2,670
Total senior and subordinated notes	1,637	3,039	3,631	587	4,384	5,256	18,534	13,134
Other long-term borrowings:								
FHLB advances	1,013	6	35	12	3	2	1,071	1,016
Total long-term debt ⁽¹⁾	3,015	6,143	9,498	599	5,525	5,333	30,113	24,439
Total short-term borrowings and long-term debt	\$15,145	\$6,143	\$9,498	\$599	\$5,525	\$5,333	\$42,243	\$40,654
Percentage of total	36	% 15	% 22	% 1	% 13	% 13	% 100	%

⁽¹⁾ Includes unamortized discounts, premiums and other cost basis adjustments, which together result in a net reduction of \$237 million and \$236 million as of September 30, 2014 and December 31, 2013, respectively.

We provide additional information on our short-term borrowings and long-term debt under “Consolidated Balance Sheets Analysis—Securitized Debt Obligations,” “Consolidated Balance Sheet Analysis—Other Debt” and in “Note 8—Deposits and Borrowings.”

Borrowing Capacity

Under our shelf registration statement filed with the U.S. Securities and Exchange Commission on April 30, 2012, from time to time, we may offer and sell an indeterminate aggregate amount of senior or subordinated debt securities, preferred stock, depository shares, common stock, purchase contracts, warrants and units. There is no limit under this shelf registration statement to the amount or number of such securities that we may offer and sell, subject to market conditions. Our current shelf registration statement will expire three years from the filing date.

In addition to our issuance capacity under the shelf registration statement, we also have access to FHLB advances with a maximum borrowing capacity of \$37.8 billion as of September 30, 2014. This borrowing capacity was secured by posting \$30.5 billion of loans and \$7.3 billion of securities as collateral. As of September 30, 2014, we had

outstanding FHLB advances and letters of credit of \$11.3 billion, and \$26.5 billion still available to us to borrow under this program. The ability to draw down funding is based on membership status and the amount is dependent upon the Banks' ability to post collateral. Our FHLB membership is secured by our investment in FHLB stock of \$519 million and \$774 million as of September 30, 2014 and December 31, 2013, respectively, which are determined in part based on our outstanding advances. We also have access to the Federal Reserve Discount Window but did not utilize this funding source during 2014 or 2013 outside of standard operational testing.

Credit Ratings

Our credit ratings have a significant impact on our ability to access capital markets and our non-deposit borrowing costs. Rating agencies base their ratings on numerous factors, including liquidity, capital adequacy, asset quality, quality of earnings and the

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probability of systemic support. Significant changes in these factors could result in different ratings. Such ratings help to support our cost effective unsecured funding as part of our overall financing programs. Table 32 provides a summary of the credit ratings for the senior unsecured debt of Capital One Financial Corporation, COBNA and CONA as of September 30, 2014 and December 31, 2013.

Table 32: Senior Unsecured Debt Credit Ratings

	September 30, 2014			December 31, 2013		
	Capital One Financial Corporation	Capital One Bank (USA), N.A.	Capital One, N.A.	Capital One Financial Corporation	Capital One Bank (USA), N.A.	Capital One, N.A.
Moody's	Baa1	A3	A3	Baa1	A3	A3
S&P	BBB	BBB+	BBB+	BBB	BBB+	BBB+
Fitch	A-	A-	A-	A-	A-	A-

As of October 31, 2014, Moody's, S&P and Fitch have us on a stable outlook.

MARKET RISK PROFILE

Market risk is inherent in the financial instruments associated with our operations and activities, including loans, deposits, securities, short-term borrowings, long-term debt and derivatives. Below we provide additional information about our primary sources of market risk, our market risk management strategies and the measures we use to evaluate our market risk exposure.

Primary Market Risk Exposures

Our primary source of market risk is interest rate risk. We also have exposure to foreign exchange risk.

Interest Rate Risk

Interest rate risk, which represents exposure to instruments whose yield or price varies with the volatility of interest rates, is our most significant source of market risk exposure. Banks are inevitably exposed to interest rate risk due to differences in the timing between the maturities or repricing of assets and liabilities.

Foreign Exchange Risk

Foreign exchange risk represents exposure to changes in the values of current holdings and future cash flows denominated in other currencies. Changes in foreign exchange rates affect the reported earnings of our foreign operations and the value of non-dollar denominated equity invested in those foreign operations affect our AOCI and capital ratios. We measure our total exposure by regularly tracking the value of our net equity invested in our foreign operations as well as their funding requirements. As of September 30, 2014, our pre-tax earnings, AOCI and capital ratios exposures to volatility of foreign exchange rates was minimal.

Market Risk Management

We employ several techniques to manage our interest rate and foreign exchange risk, which include, but are not limited to, altering the duration and re-pricing characteristics of our various assets and liabilities through interest rate derivatives or mitigating the foreign exchange exposure of certain non-dollar denominated equity or transactions through derivatives. We execute our derivative contracts in both over-the-counter and exchange-traded derivative markets. Although the majority of our derivatives are interest rate swaps, we also use a variety of other derivative instruments, including caps, floors, options, futures and forward contracts, to manage both our interest rate and foreign currency risk. The outstanding notional amount of our derivative contracts totaled \$81.5 billion as of September 30, 2014, compared with \$63.4 billion as of December 31, 2013.

Market Risk Measurement

We have prescribed risk management policies and limits established by our Market and Liquidity Risk Policy and approved by the Board of Directors. Our objective is to manage our asset/liability risk position and exposure to market risk in accordance with these policies and prescribed limits based on prevailing market conditions and long-term expectations. Because no single measure can reflect all aspects of market risk, we use various industry standard market risk measurement techniques and analyses to measure,

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assess and manage the impact of changes in interest rates on our net interest income and our economic value of equity and foreign exchange rates on our non-dollar denominated earnings and non-dollar equity investments in foreign operations. We provide additional information below in “Economic Value of Equity.”

We consider the impact on both net interest income and economic value of equity in measuring and managing our interest rate risk. Because the federal funds rate was lowered to near zero in December 2008 and since then has remained in a target range of 0% to 0.25%, we use a 50 basis point decrease as our declining interest rate scenario, since a scenario where interest rates would decline by 200 basis points is unlikely. In scenarios where a 50 basis point decline would result in a rate less than 0%, we assume a rate of 0%. Below we discuss the assumptions used in calculating each of these measures.

Net Interest Income Sensitivity

This sensitivity measure estimates the impact on our projected 12-month base-line interest rate sensitive revenue resulting from movements in interest rates. Interest rate sensitive revenue consists of net interest income and certain components of other non-interest income significantly impacted by movements in interest rates, including changes in the fair value of mortgage servicing rights and free-standing interest rate swaps. In addition to our existing assets and liabilities, we incorporate expected future business growth assumptions, such as loan and deposit growth and pricing, and plans for projected changes in our funding mix in our baseline forecast. In measuring the sensitivity of interest rate movements on our projected interest rate sensitive revenue, we assume an instantaneous plus 200 basis point and minus 50 basis point shock, with the lower rate scenario limited to zero as described above.

Economic Value of Equity

Our economic value of equity sensitivity measure estimates the impact on the net present value of our assets and liabilities, including derivative hedging activity, resulting from movements in interest rates. Our economic value of equity sensitivity measures are calculated based on our existing assets and liabilities, including derivatives, and do not incorporate business growth assumptions or projected plans for funding mix changes. In measuring the sensitivity of interest rate movements on our economic value of equity, we assume a hypothetical instantaneous parallel shift in the level of interest rates of plus 200 basis points and minus 50 basis points to spot rates, with the lower rate scenario limited to zero as described above.

Table 33 shows the estimated percentage impact on our projected base-line interest rate sensitive revenue and economic value of equity, calculated under the hypothetical interest rate scenarios described above, as of September 30, 2014 and December 31, 2013. In addition to these industry standard measures, we will continue to factor into our internal interest rate risk management decisions the potential impact of alternative interest rate scenarios, such as stressed rate shocks as well as steepening and flattening yield curve scenarios.

Table 33: Interest Rate Sensitivity Analysis

	September 30, 2014	December 31, 2013
Impact on projected base-line net interest income:		
+200 basis points	3.4	% 4.9
-50 basis points	(1.6)	) (1.5)
Impact on economic value of equity:		
+200 basis points	(5.2)	) (5.7)
-50 basis points	(0.4)	) 0.3

Our projected net interest income and economic value of equity sensitivity measures were within our prescribed policy limits as of September 30, 2014 and December 31, 2013.

Limitations of Market Risk Measures

The interest rate risk models that we use in deriving these measures incorporate contractual information, internally-developed assumptions and proprietary modeling methodologies, which project borrower and depositor behavior patterns in certain interest rate environments. Other market inputs, such as interest rates, market prices and interest rate volatility, are also critical components of our interest rate risk measures. We regularly evaluate, update and enhance these assumptions, models and analytical tools as

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we believe appropriate to reflect our best assessment of the market environment and the expected behavior patterns of our existing assets and liabilities.

There are inherent limitations in any methodology used to estimate the exposure to changes in market interest rates. The above sensitivity analysis contemplates only certain movements in interest rates and is performed at a particular point in time based on the existing balance sheet and, in some cases, expected future business growth and funding mix assumptions. The strategic actions that management may take to manage our balance sheet may differ significantly from our projections, which could cause our actual earnings and economic value of equity sensitivities to differ substantially from the above sensitivity analysis.

SUPERVISION AND REGULATION

Basel III and U.S. Capital Rules

On September 3, 2014, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (the “Federal Banking Agencies”) issued final rules implementing the Basel III liquidity coverage ratio in the United States. The rule (the “Final LCR Rule”) applies to institutions with \$250 billion or more in total consolidated assets or \$10 billion or more in total consolidated on-balance sheet foreign exposure, and their respective consolidated subsidiary depository institutions with \$10 billion or more in total consolidated assets. As a result, the Company and the Banks are subject to the Final LCR Rule. The Final LCR Rule will require the Company and each of the Banks to hold an amount of eligible high-quality, liquid assets that equals or exceeds 100% of their respective projected net cash outflows over a 30-day period, each as calculated in accordance with the Final LCR Rule. The Final LCR Rule phases in the minimum liquidity coverage ratio (or “LCR”) standard as follows: 80% by January 1, 2015; 90% by January 1, 2016; and 100% by January 1, 2017 and thereafter. The Final LCR Rule takes effect in January 2015 and requires us to calculate the LCR as of the last business day of each month from January 2015 until July 2016. As of July 1, 2016, the Final LCR Rule requires us to calculate the LCR on a daily basis. We expect to meet the requirements of the first phase of the Final LCR Rule when it takes effect in January 2015. Over the course of 2014, we have been modifying the composition of our investment portfolio in preparation for the Final LCR Rule, with some of these actions resulting in us purchasing types of securities that are lower yielding than securities we would otherwise be purchasing if not for the Final LCR Rule. In July 2013, the Federal Banking Agencies issued a rule implementing the Basel III capital framework (the “Final Basel III Capital Rules”) developed by the Basel Committee on Banking Supervision (the “Basel Committee”) as well as certain Dodd-Frank Act and other capital provisions. For advanced approaches institutions like the Company and Banks, the Final Basel III Capital Rules included a supplementary leverage ratio based upon the Basel III leverage ratio. On September 3, 2014, the Federal Banking Agencies issued a final rule that revised the supplementary leverage ratio consistent with revisions made by the Basel Committee to the leverage ratio, including, among other changes, modifying the methodology for including off-balance sheet items in the denominator of the supplementary leverage ratio (the denominator referred to as “total leverage exposure”). The final rule also requires institutions to calculate total leverage exposure using daily averages for on-balance sheet items and the average of three month-end calculations for off-balance sheet items. The Company must make publicly available certain disclosures regarding its supplementary leverage ratio in the first quarter of 2015, including information summarizing the differences between the total consolidated assets reported in its published financial statements and regulatory reports and total leverage exposure for purposes of calculating its supplementary coverage ratio. The supplementary leverage ratio becomes effective January 1, 2018.

Capital Planning and Stress Testing

On October 17, 2014, the Federal Reserve issued a final rule to modify the regulations for capital planning and stress testing (the “Final Rule”). The Final Rule changes the annual capital plan and stress test cycle start date from October 1 to January 1, effective for the cycle beginning January 1, 2016. In order to provide a transition to the change in timing, the Federal Reserve’s decision on a bank holding company’s (“BHC”) 2015 capital plan submission would cover a five-quarter period—from the second quarter of 2015 through the second quarter of 2016. Subsequent submissions each would cover a four-quarter period.

The change in the start date of the annual cycle impacts the as-of dates for data used to project results as well as the dates that stress test results must be submitted to the regulators and disclosed to the public. For the annual company-run stress test, a BHC is required to disclose the results within 15 calendar days after the Federal Reserve discloses the results of that BHC's supervisory stress test, unless that time was extended by the Federal Reserve. The Final Rule requires a BHC to disclose results of its mid-

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cycle stress test within 30 calendar days after the BHC submits the results of its mid-cycle stress test to the Federal Reserve, unless that time period is extended by the Federal Reserve.

The Final Rule also provides a one-year deferral on the use of advanced approaches methodology and will not require banking institutions that have exited parallel run to use the advanced approaches methodology to estimate their capital ratios for the 2015 capital plan and stress test cycles.

In addition, the Final Rule shifts the Federal Reserve’s focus from annual capital issuances and distributions to quarterly capital issuances and distributions by establishing a new cumulative net distribution requirement. With certain limited exceptions, this requirement provides that—as measured on an aggregate basis beginning in the third quarter of the planning horizon—to the extent a BHC does not issue the amount of a given class of regulatory capital instrument that it projected in its capital plan, the BHC must reduce its capital distributions as required by the Final Rule such that the cumulative net amounts of a BHC’s actual capital issuances and capital distributions for that category of regulatory capital instrument cannot be less than the cumulative net amounts of capital issuances and capital distributions projected in the BHC’s capital plan for that category of regulatory capital instrument.

We provide additional information on our Supervision and Regulation in our 2013 Form 10-K under “Part I—Item 1—Business—Supervision and Regulation” and in our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2014, and June 30, 2014 under “Part I—Item 2—Management Discussion and Analysis of Financial Condition and Results of Operations—Supervision and Regulation.”

FORWARD-LOOKING STATEMENTS

From time to time, we have made and will make forward-looking statements, including those that discuss, among other things, strategies, goals, outlook or other non-historical matters; projections, revenues, income, returns, expenses, capital measures, accruals for claims in litigation and for other claims against us, earnings per share or other financial measures for us; future financial and operating results; our plans, objectives, expectations and intentions; and the assumptions that underlie these matters.

To the extent that any such information is forward-looking, it is intended to fit within the safe harbor for forward-looking information provided by the Private Securities Litigation Reform Act of 1995.

Numerous factors could cause our actual results to differ materially from those described in such forward-looking statements, including, among other things:

- general economic and business conditions in the U.S., the U.K., Canada or our local markets, including conditions affecting employment levels, interest rates, consumer income and confidence, spending and savings that may affect consumer bankruptcies, defaults, charge-offs and deposit activity;
- an increase or decrease in credit losses (including increases due to a worsening of general economic conditions in the credit environment);
- financial, legal, regulatory, tax or accounting changes or actions, including the impact of the Dodd-Frank Act and the regulations promulgated thereunder and regulations governing bank capital and liquidity standards, including Basel-related initiatives and potential changes to financial accounting and reporting standards;
- developments, changes or actions relating to any litigation matter involving us;
- the inability to sustain revenue and earnings growth;
- increases or decreases in interest rates;
- our ability to access the capital markets at attractive rates and terms to capitalize and fund our operations and future growth;
- the success of our marketing efforts in attracting and retaining customers;
- increases or decreases in our aggregate loan balances or the number of customers and the growth rate and composition thereof, including increases or decreases resulting from factors such as shifting product mix, amount of actual marketing expenses we incur and attrition of loan balances;

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the level of future repurchase or indemnification requests we may receive, the actual future performance of mortgage loans relating to such requests, the success rates of claimants against us, any developments in litigation and the actual recoveries we may make on any collateral relating to claims against us;

the amount and rate of deposit growth;

changes in the reputation of, or expectations regarding, the financial services industry or us with respect to practices, products or financial condition;

any significant disruption in our operations or technology platform;

- our ability to maintain a compliance infrastructure suitable for the nature of our business;

our ability to control costs;

the amount of, and rate of growth in, our expenses as our business develops or changes or as it expands into new market areas;

our ability to execute on our strategic and operational plans;

- any significant disruption of, or loss of public confidence in, the United States Mail service affecting our response rates and consumer payments;

any significant disruption of, or loss of public confidence in, the internet affecting the ability of our customers to access their accounts and conduct banking transactions;

our ability to recruit and retain experienced personnel to assist in the management and operations of new products and services;

changes in the labor and employment markets;

fraud or misconduct by our customers, employees or business partners;

competition from providers of products and services that compete with our businesses; and

other risk factors listed from time to time in reports that we file with the SEC.

Any forward-looking statements made by us or on our behalf speak only as of the date they are made or as of the date indicated, and we do not undertake any obligation to update forward-looking statements as a result of new information, future events or otherwise. You should carefully consider the factors discussed above in evaluating these forward-looking statements. For additional information on factors that could materially influence forward-looking statements included in this Report, see the risk factors set forth under “Part II—Item 1A. Risk Factors” in this Report and in “Part I—Item 1A. Risk Factors” in our 2013 Form 10-K.

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SUPPLEMENTAL TABLES

Table A—Reconciliation of Non-GAAP Measures and Calculation of Regulatory Capital Measures

(Dollars in millions)	September 30, 2014	December 31, 2013
Tangible Common Equity (Quarterly Average)		
Average stockholders' equity	\$ 44,827	\$ 42,355
Adjustments:		
Average goodwill and other intangible assets ⁽²⁾	(15,525)	(15,847)
Noncumulative perpetual preferred stock ⁽³⁾	(1,338)	(853)
Average tangible common equity	\$ 27,964	\$ 25,655
Tangible Common Equity (Period End)		
End of period stockholders' equity	\$ 44,018	\$ 41,632
Adjustments:		
Goodwill and other intangible assets ⁽²⁾	(15,472)	(15,784)
Noncumulative perpetual preferred stock ⁽³⁾	(1,336)	(853)
Tangible common equity	\$ 27,210	\$ 24,995
Tangible Assets (Quarterly Average)		
Average assets	\$ 299,523	\$ 294,040
Adjustments: Average goodwill and other intangible assets ⁽²⁾	(15,525)	(15,847)
Average tangible assets	\$ 283,998	\$ 278,193
Tangible Assets (Period End)		
End of period assets	\$ 300,202	\$ 296,933
Adjustments: Goodwill and other intangible assets ⁽²⁾	(15,472)	(15,784)
Tangible assets	\$ 284,730	\$ 281,149
Non-GAAP TCE ratio		
TCE ratio ⁽⁴⁾	9.56	% 8.89
Capital Ratios ⁽⁵⁾		
Common equity Tier 1 capital ratio ⁽⁶⁾	12.73	% N/A
Tier 1 common ratio ⁽⁷⁾	N/A	12.19
Tier 1 risk-based capital ratio ⁽⁸⁾	13.31	% 12.57
Total risk-based capital ratio ⁽⁹⁾	15.24	14.69
Tier 1 leverage ratio ⁽¹⁰⁾	10.64	10.06
Risk-weighted assets ⁽¹¹⁾	\$ 228,759	\$ 224,556
Average assets for the leverage ratio	286,070	280,574

(Dollars in millions)	September 30, 2014
Regulatory Capital Ratios Under Basel III Standardized Approach ⁽⁵⁾	
Common equity excluding AOCI	\$ 43,241
Adjustments:	
AOCI ⁽¹²⁾⁽¹³⁾	(146)
Goodwill ⁽²⁾	(13,801)
Intangible Assets ⁽²⁾⁽¹³⁾	(266)
Other	88
Common equity Tier 1 capital	29,116
Tier 1 capital instruments ⁽³⁾	1,336
Additional Tier 1 capital adjustments	(1)
Tier 1 capital	30,451

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(Dollars in millions)	September 30, 2014
Tier 2 capital instruments ⁽³⁾	1,530
Qualifying allowance for loan and lease losses	2,878
Additional Tier 2 capital adjustments	1
Tier 2 capital	4,409
Total risk-based capital ⁽¹⁴⁾	\$34,860
(Dollars in millions)	December 31, 2013
Regulatory Capital Ratios Under Basel I ⁽⁵⁾	
Total stockholders' equity	\$ 41,632
Adjustments:	
Net unrealized losses on investment securities available for sale recorded in AOCI ⁽¹²⁾	791
Net losses on cash flow hedges recorded in AOCI ⁽¹²⁾	136
Disallowed goodwill and other intangible assets ⁽²⁾	(14,326)
Disallowed deferred tax assets	—
Noncumulative perpetual preferred stock ⁽³⁾	(853)
Other	(5)
Tier 1 common capital	27,375
Noncumulative perpetual preferred stock ⁽³⁾	853
Tier 1 restricted core capital items	2
Tier 1 capital	28,230
Long-term debt qualifying as Tier 2 capital	1,914
Qualifying allowance for loan and lease losses	2,833
Other Tier 2 components	10
Tier 2 capital	4,757
Total risk-based capital ⁽¹⁴⁾	\$ 32,987

In the first quarter of 2014, we adopted the proportional amortization method of accounting for Investments in

- (1) Qualified Affordable Housing Projects. See "Note 1—Summary of Significant Accounting Policies" for additional information. Prior periods have been recast to conform to this presentation.
- (2) Includes impact of related deferred taxes.
- (3) Includes related surplus.
- (4) TCE ratio is a non-GAAP measure calculated based on tangible common equity divided by tangible assets.
- (5) Beginning on January 1, 2014, we calculate our regulatory capital under the Basel III Standardized Approach subject to transition provisions. Prior to January 1, 2014, we calculated regulatory capital under Basel I.
- (6) Common equity Tier 1 capital ratio is a regulatory capital measure calculated based on common equity Tier 1 capital divided by risk-weighted assets.
- (7) Tier 1 common capital ratio is a regulatory capital measure under Basel I calculated based on Tier 1 common capital divided by Basel I risk-weighted assets.
- (8) Tier 1 risk-based capital ratio is a regulatory capital measure calculated based on Tier 1 capital divided by risk-weighted assets.
- (9) Total risk-based capital ratio is a regulatory capital measure calculated based on total risk-based capital divided by risk-weighted assets.
- (10) Tier 1 leverage ratio is a regulatory capital measure calculated based on Tier 1 capital divided by average assets, after certain adjustments.
- (11) Risk-weighted assets continue to be calculated based on Basel I in 2014.
- (12) Amounts presented are net of tax.

(13) Amounts based on transition provisions for regulatory capital deductions and adjustments of 20% for 2014.

(14) Total risk-based capital equals the sum of Tier 1 capital and Tier 2 capital.

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Glossary and Acronyms

2012 U.S. card acquisition: On May 1, 2012, pursuant to the agreement with HSBC Finance Corporation, HSBC USA Inc. and HSBC Technology and Services (USA) Inc. (collectively, “HSBC”), we closed the acquisition of substantially all of the assets and assumed liabilities of HSBC’s credit card and private label credit card business in the United States (other than the HSBC Bank USA, consumer credit card program and certain other retained assets and liabilities).

Acquired Loans: A limited portion of the credit card loans acquired in the 2012 U.S. card acquisition and the substantial majority of consumer and commercial loans acquired in the ING Direct and Chevy Chase Bank acquisitions, which were recorded at fair value at acquisition and subsequently accounted for based on expected cash flows to be collected (under the accounting standard formerly known as “Statement of Position 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer,” commonly referred to as “SOP 03-3”). The difference between the fair value at acquisition and expected cash flows represents the accretable yield, which is recognized into interest income over the life of the loans. The difference between the contractual payments on the loans and expected cash flows represents the nonaccretable difference or the amount of principal and interest not considered collectible, which incorporates future expected credit losses over the life of the loans. Decreases in expected cash flows from the previous estimate resulting from further credit deterioration will generally result in an impairment charge recognized in our provision for credit losses and an increase in the allowance for loan and lease losses. Charge-offs are not recorded until the expected credit losses within the nonaccretable difference is depleted. In addition, Acquired Loans are not classified as delinquent or nonperforming as we expect to collect our net investment in these loans and the nonaccretable difference will absorb the majority of the losses associated with these loans.

Annual Report: References to our “2013 Form 10-K” or “2013 Annual Report” are to our “Annual Report” on Form 10-K for the fiscal year ended December 31, 2013.

Banks: Refers to COBNA and CONA.

Basel Committee: The Basel Committee on Banking Supervision.

Benefit Obligation and Projected Benefit Obligation: Benefit Obligation refers to the total of the projected benefit obligation for pension plans and the accumulated postretirement benefit obligations. Projected Benefit Obligation represents the actuarial present value of all benefits accrued on employee service rendered prior to the calculation date, including allowance for future salary increases if the pension benefit is based on future compensation levels.

BHC Act: The Bank Holding Company Act of 1956, as amended (12 U.S.C. § 1842).

Capital One: Capital One Financial Corporation and its subsidiaries.

Carrying Value (with respect to loans): The amount at which a loan is recorded on the balance sheet. For loans recorded at amortized cost, carrying value is the unpaid principal balance net of unamortized deferred loan origination fees and costs, and unamortized purchase premium or discount. For loans that are or have been on nonaccrual status, the carrying value is also reduced by any net charge-offs that have been recorded and the amount of interest payments applied as a reduction of principal under the cost recovery method. For credit card loans, the carrying value also includes interest that has been billed to the customer. For loans classified as held for sale, carrying value is the lower of carrying value as described in the sentences above, or fair value. For Acquired Loans, the carrying value equals fair value upon acquisition adjusted for subsequent cash collections and yield accreted to date.

CCB: Chevy Chase Bank, F.S.B., which was acquired by the Company on February 27, 2009.

COBNA: Capital One Bank (USA), National Association, one of our fully owned subsidiaries, which offers credit and debit card products, other lending products and deposit products.

Collective trusts: An investment fund formed from the pooling of investments by investors.

Common Equity Tier 1 Capital: Common Equity, related surplus, and retained earnings less accumulated other comprehensive income net of applicable phase-ins, less goodwill and intangibles net of associated deferred tax liabilities and applicable phase-ins, less other deductions, as defined by regulators.

Company: Capital One Financial Corporation and its subsidiaries.

CONA: Capital One, National Association, one of our fully owned subsidiaries, which offers a broad spectrum of banking products and financial services to consumers, small businesses and commercial clients.

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Credit derivatives: Contractual agreements that provide insurance against a credit event of one or more referenced credits. Such events include bankruptcy, insolvency and failure to meet payment obligations when due.

Credit risk: Credit risk is the risk of loss from an obligor's failure to meet the terms of any contract or otherwise fail to perform as agreed.

Derivative: A contract or agreement whose value is derived from changes in interest rates, foreign exchange rates, prices of securities or commodities, credit worthiness for credit default swaps or financial or commodity indices.

Discontinued operations: The operating results of a component of an entity, as defined by ASC 205, that are removed from continuing operations when that component has been disposed of or it is management's intention to sell the component.

Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"): Regulatory reform legislation signed into law on July 21, 2010. This law broadly affects the financial services industry and contains numerous provisions aimed at strengthening the sound operation of the financial services sector.

Exchange Act: The Securities Exchange Act of 1934.

eXtensible Business Reporting Language ("XBRL"): A language for the electronic communication of business and financial data.

FICO Score: A measure of consumer credit risk provided by credit bureaus, typically produced from statistical modeling software created by Fair Isaac Corporation utilizing data collected by the credit bureaus.

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

Final Basel III Capital Rules: The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency issued a rule implementing the Basel III capital framework developed by the Basel Committee on Banking Supervision as well as certain Dodd-Frank Act and other capital provisions.

Final LCR Rule: The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency issued final rules implementing the Basel III liquidity coverage ratio in the United States.

Final Rule: A new capital rule finalized by the Federal Reserve, the OCC and the FDIC (collectively, the U.S. federal banking agencies) that implements the Basel III capital accord developed by the Basel Committee on Banking Supervision and incorporates certain Dodd-Frank Act capital provisions and updates to the PCA capital requirements.

Foreign currency swaps: An agreement to exchange contractual amounts of one currency for another currency at one or more future dates.

Foreign exchange contracts: Contracts that provide for the future receipt or delivery of foreign currency at previously agreed-upon terms.

Forward rate agreements: Contracts to exchange payments on a specified future date, based on a market change in interest rates from trade date to contract settlement date.

GreenPoint: Refers to our wholesale mortgage banking unit, GreenPoint Mortgage Funding, Inc. ("GreenPoint"), which was closed in 2007.

GSE or Agency: A government-sponsored enterprise or agency is a financial services corporation created by the United States Congress. Examples of U.S. government agencies include Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac), Government National Mortgage Association (Ginnie Mae) and the Federal Home Loan Banks.

Impairment: The condition when the carrying amount of an asset exceeds or is expected to exceed its fair value.

Impaired loans: A loan is considered impaired when, based on current information and events, it is probable that we will not be able to collect all amounts due from the borrower in accordance with the original contractual terms of the loan.

Inactive Insured Securitizations: Securitizations as to which the monoline bond insurers have not made repurchase requests or loan file requests to one of our subsidiaries.

ING Direct acquisition: On February 17, 2012, we completed the acquisition of substantially all of the ING Direct business in the United States ("ING Direct") from ING Groep N.V., ING Bank N.V., ING Direct N.V. and ING Direct

Bancorp.

Insured Securitizations: Securitizations supported by bond insurance.

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Capital One Financial Corporation
(COF)

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Interest rate sensitivity: The exposure to interest rate movements.

Interest rate swaps: Contracts in which a series of interest rate flows in a single currency are exchanged over a prescribed period. Interest rate swaps are the most common type of derivative contract that we use in our asset/liability management activities.

Investment grade: Represents Moody's long-term rating of Baa3 or better; and/or a Standard & Poor's, Fitch or DBRS long-term rating of BBB- or better; or if unrated, an equivalent rating using our internal risk ratings. Instruments that fall below these levels are considered to be non-investment grade.

Investments in Qualified Affordable Housing Projects: Capital One invests in private investment funds that make equity investments in multifamily affordable housing properties, that provide affordable housing tax credits for these investments. The activities of these entities are financed with a combination of invested equity capital and debt.

Investor Entities: Entities that invest in community development entities ("CDE") that provide debt financing to businesses and non-profit entities in low-income and rural communities.

Leverage ratio (Basel I guideline): Tier 1 capital divided by average assets after certain adjustments, as defined by the regulators.

Liquidity risk: Liquidity risk is the risk that the Company will not be able to meet its future financial obligations as they come due, or invest in future asset growth because of an inability to obtain funds at a reasonable price within a reasonable time period.

Loan-to-value ("LTV") ratio: The relationship expressed as a percentage, between the principal amount of a loan and the appraised value of the collateral (i.e., residential real estate, autos, etc.) securing the loan.

Managed basis: A non-GAAP presentation of financial results that includes reclassifications to present revenue on a fully taxable-equivalent basis. Management uses this non-GAAP financial measure at the segment level, because it believes this provides information to enable investors to understand the underlying operational performance and trends of the particular business segment and facilitates a comparison of the business segment with the performance of competitors.

Market risk: Market risk is the risk that an institution's earnings or the economic value of equity could be adversely impacted by changes in interest rates, foreign exchange rates, or other market factors.

Master netting agreement: An agreement between two counterparties that have multiple contracts with each other that provides for the net settlement of all contracts through a single payment in the event of default or termination of any one contract.

Mortgage-Backed Security ("MBS"): An asset-backed security whose cash flows are backed by the principal and interest payments of a set of mortgage loans.

Mortgage Servicing Rights ("MSR"): The right to service a mortgage loan when the underlying loan is sold or securitized. Servicing includes collections for principal, interest and escrow payments from borrowers and accounting for and remitting principal and interest payments to investors.

Net interest margin: The result of dividing net interest revenue by average interest-earning assets.

Nonperforming loans and leases: Loans and leases that have been placed on non-accrual status.

Operational risk: The risk of loss, capital impairment, adverse customer experience, or reputational impact resulting from failure to comply with policies and procedures, failed internal processes or systems, or from external events.

Option-ARM Loans: The option-ARM real estate loan product is an adjustable-rate mortgage loan that provides the borrower with the option each month to make a fully amortizing, interest-only or minimum payment.

Other-than-temporary impairment ("OTTI"): An impairment charge taken on a security whose fair value has fallen below the carrying value on the balance sheet and its value is not expected to recover through the holding period of the security.

Patriot Act: The USA PATRIOT Act of 2001 (Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism).

Portfolio Sale: The sale of the Best Buy private label and co-branded credit card portfolio to Citibank, N.A., which was completed on September 6, 2013.

Proxy Statement: Capital One's Proxy Statement for the 2014 Annual Stockholders Meeting.

Public Fund deposits: Deposits that are derived from a variety of political subdivisions such as school districts and municipalities.

Purchase volume: Dollar amount of customer purchases, net of returns.

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Rating Agency: An independent agency that assesses the credit quality and likelihood of default of an issue or issuer and assigns a rating to that issue or issuer.

Repurchase Agreement: An instrument used to raise short term funds whereby securities are sold with an agreement for the seller to buy back the securities at a later date.

Restructuring charges: Charges typically from the consolidation and/or relocation of operations.

Return on assets: Calculated based on annualized income from continuing operations, net of tax, for the period divided by average total assets for the period.

Return on common equity: Calculated based on the annualized sum of (i) income from continuing operations, net of tax; (ii) less dividends and undistributed earnings allocated to participating securities; (iii) less preferred stock dividends, for the period, divided by average common equity. Our calculation of return on average common equity may not be comparable to similarly titled measures reported by other companies.

Return on tangible common equity: Calculated based on the annualized sum of (i) income from continuing operations, net of tax; (ii) less dividends and undistributed earnings allocated to participating securities; (iii) less preferred stock dividends, for the period, divided by average tangible common equity. Our calculation of return on average tangible common equity may not be comparable to similarly titled measures reported by other companies.

Risk-weighted assets: Risk-weighted assets consist of on- and off-balance sheet assets that are assigned to one of several broad risk categories and weighted by factors representing their risk and potential for default. In 2014, the calculation of risk weighted assets is based on the general risk-based approach, as defined by regulators.

Securitized Debt Obligations: A type of asset-backed security and structured credit product constructed from a portfolio of fixed-income assets.

SOP 03-3: Statement of Position 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer.

Small-ticket commercial real estate: Our small-ticket commercial real estate portfolio is predominantly low, or no documentation loans, with balances generally less than \$2 million. This portfolio was originated on a national basis through a broker network, and is in a run-off mode.

Subprime: For purposes of lending in our Credit Card business we generally consider FICO scores of 660 or below, or other equivalent risk scores, to be subprime. For purposes of auto lending in our Consumer Banking business we generally consider borrowers FICO scores of 620 or below to be subprime.

Tangible common equity ("TCE"): Common equity less goodwill and intangible assets adjusted for deferred tax liabilities associated with non-tax deductible intangible assets and tax deductible goodwill.

Tier 1 Common Capital: Tier 1 capital less preferred stock, qualifying trust preferred securities, hybrid securities and qualifying noncontrolling interest in subsidiaries under Basel I.

Troubled debt restructuring ("TDR"): A TDR is deemed to occur when the Company modifies the contractual terms of a loan agreement by granting a concession to a borrower that is experiencing financial difficulty.

U.S. federal banking agencies: The Federal Reserve, the OCC and the FDIC.

U.S. GAAP: Accounting principles generally accepted in the United States of America. Accounting rules and conventions defining acceptable practices in preparing financial statements in the U.S.

Unfunded commitments: Legally binding agreements to provide a defined level of financing until a specified future date.

Variable Interest Entity ("VIE"): An entity that: (1) lacks enough equity investment at risk to permit the entity to finance its activities without additional financial support from other parties; (2) has equity owners that lack the right to make significant decisions affecting the entity's operations; and/or (3) has equity owners that do not have an obligation to absorb or the right to receive the entity's losses or return.

Acronyms

ABS: Asset-backed securities

AOCI: Accumulated other comprehensive income

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ARM: Adjustable rate mortgage
Bps: Basis points
CCAR: Comprehensive Capital Analysis and Review
CDE: Community development entities
CFPB: Consumer Financial Protection Bureau
CFTC: Commodity Futures Trading Commission
CMBS: Commercial mortgage-backed securities
COEP: Capital One (Europe) plc
COF: Capital One Financial Corporation
COSO: Committee of Sponsoring Organizations of the Treadway Commission
CRA: Community Reinvestment Act
DUS: Delegated underwriter and servicing
Fannie Mae: Federal National Mortgage Association
FASB: Financial Accounting Standards Board
FCA: U.K. Financial Conduct Authority
FDIC: Federal Deposit Insurance Corporation
FDICIA: The Federal Deposit Insurance Corporation Improvement Act of 1991
FFIEC: Federal Financial Institutions Examination Council
FHA: Federal Housing Administration
FHLB: Federal Home Loan Banks
FICO: Fair Isaac Corporation (credit rating)
FIRREA: Financial Institutions Reform, Recovery, and Enforcement Act
Fitch: Fitch Ratings
Freddie Mac: Federal Home Loan Mortgage Corporation
FTE: Fully taxable-equivalent
FVC: Fair Value Committee
GDP: Gross domestic product
Ginnie Mae: Government National Mortgage Association
GSE or Agencies: Government Sponsored Enterprise
HBC: Hudson Bay Company
HELOCs: Home Equity Lines of Credit
HFI: Held for Investment
HSBC: HSBC Finance Corporation, HSBC USA Inc. and HSBC Technology and Services (USA) Inc.
LCR: Liquidity Coverage Ratio
LIBOR: London Interbank Offered Rate
Moody's: Moody's Investors Service
NOW: Negotiable order of withdrawal
OCC: Office of the Comptroller of the Currency
OIS: Overnight Indexed Swap
OTC: Over-the-counter
PCA: Prompt corrective action
PCCR: Purchased credit card relationship
RMBS: Residential mortgage-backed securities

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S&P: Standard & Poor's

SCRA: Servicemembers Civil Relief Act

SEC: U.S. Securities and Exchange Commission

TARP: Troubled Asset Relief Program

TAV: Trade Analytics and Valuation team

TCE: Tangible Common Equity

TILA: Truth in Lending Act

UCL: Unfair Competition Law

VAC: Valuations Advisory Committee

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Item 1. Financial Statements and Notes

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CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Three Months		Nine Months Ended	
	Ended September 30,		September 30,	
(Dollars in millions, except per share-related data)	2014	2013	2014	2013
Interest income:				
Loans, including loans held for sale	\$4,463	\$4,579	\$13,049	\$13,824
Investment securities	398	396	1,223	1,161
Other	26	23	80	74
Total interest income	4,887	4,998	14,352	15,059
Interest expense:				
Deposits	271	309	819	953
Securitized debt obligations	32	42	109	143
Senior and subordinated notes	71	76	226	240
Other borrowings	16	11	36	40
Total interest expense	390	438	1,190	1,376
Net interest income	4,497	4,560	13,162	13,683
Provision for credit losses	993	849	2,432	2,496
Net interest income after provision for credit losses	3,504	3,711	10,730	11,187
Non-interest income:				
Service charges and other customer-related fees	471	530	1,405	1,614
Interchange fees, net	523	476	1,498	1,407
Total other-than-temporary impairment	(10)	(16)	(16)	(34)
Less: Portion of other-than-temporary impairment recorded in AOCI	1	5	1	(6)
Net other-than-temporary impairment recognized in earnings	(9)	(11)	(15)	(40)
Other	157	96	427	176
Total non-interest income	1,142	1,091	3,315	3,157
Non-interest expense:				
Salaries and associate benefits	1,128	1,152	3,414	3,365
Occupancy and equipment	419	376	1,271	1,104
Marketing	392	299	1,052	946
Professional services	304	328	887	990
Communications and data processing	196	225	595	677
Amortization of intangibles	130	161	409	505
Other	416	568	1,268	1,531
Total non-interest expense	2,985	3,109	8,896	9,118
Income from continuing operations before income taxes	1,661	1,693	5,149	5,226
Income tax provision	536	575	1,696	1,747
Income from continuing operations, net of tax	1,125	1,118	3,453	3,479
Loss from discontinued operations, net of tax	(44)	(13)	(24)	(210)
Net income	1,081	1,105	3,429	3,269
Dividends and undistributed earnings allocated to participating securities	(5)	(5)	(14)	(14)
Preferred stock dividends	(20)	(13)	(46)	(39)
Net income available to common stockholders	\$1,056	\$1,087	\$3,369	\$3,216
Basic earnings per common share:				
Net income from continuing operations	\$1.97	\$1.89	\$5.99	\$5.89
Loss from discontinued operations	(0.08)	(0.02)	(0.04)	(0.36)

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Net income per basic common share	\$1.89	\$1.87	\$5.95	\$5.53
Diluted earnings per common share:				
Net income from continuing operations	\$1.94	\$1.86	\$5.90	\$5.82
Loss from discontinued operations	(0.08)	(0.02)	(0.04)	(0.36)
Net income per diluted common share	\$1.86	\$1.84	\$5.86	\$5.46
Dividends paid per common share	\$0.30	\$0.30	\$0.90	\$0.65

See Notes to Consolidated Financial Statements.

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CAPITAL ONE FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

(Dollars in millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income	\$1,081	\$1,105	\$3,429	\$3,269
Other comprehensive income (loss) before taxes:				
Net unrealized gains (losses) on securities available for sale	(104)	1,107	394	(849)
Net unrealized gains (losses) on securities held to maturity	35	(1,465)	96	(1,465)
Net unrealized gains (losses) on cash flow hedges	(107)	84	37	(195)
Foreign currency translation adjustments	(41)	124	25	(19)
Other	6	(1)	2	6
Other comprehensive income (loss) before taxes	(211)	(151)	554	(2,522)
Income tax provision (benefit) related to other comprehensive income	(23)	(104)	241	(944)
Other comprehensive income (loss), net of tax	(188)	(47)	313	(1,578)
Comprehensive income	\$893	\$1,058	\$3,742	\$1,691
See Notes to Consolidated Financial Statements.				

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CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(Dollars in millions, except per share data)	September 30, 2014	December 31, 2013
Assets:		
Cash and cash equivalents:		
Cash and due from banks	\$ 2,652	\$ 2,821
Interest-bearing deposits with banks	3,212	3,131
Federal funds sold and securities purchased under agreements to resell	284	339
Total cash and cash equivalents	6,148	6,291
Restricted cash for securitization investors	405	874
Securities available for sale, at fair value	39,665	41,800
Securities held to maturity, at carrying value	22,182	19,132
Loans held for investment:		
Unsecuritized loans held for investment	165,021	157,651
Restricted loans for securitization investors	36,571	39,548
Total loans held for investment	201,592	197,199
Allowance for loan and lease losses	(4,212)	(4,315)
Net loans held for investment	197,380	192,884
Loans held for sale, at lower of cost or fair value	427	218
Premises and equipment, net	3,752	3,839
Interest receivable	1,268	1,418
Goodwill	13,970	13,978
Other assets	15,005	16,499
Total assets	\$ 300,202	\$ 296,933
Liabilities:		
Interest payable	\$ 249	\$ 307
Deposits:		
Non-interest bearing deposits	25,388	22,643
Interest-bearing deposits	178,876	181,880
Total deposits	204,264	204,523
Securitized debt obligations	10,508	10,289
Other debt:		
Federal funds purchased and securities loaned or sold under agreements to repurchase	2,330	915
Senior and subordinated notes	18,534	13,134
Other borrowings	10,871	16,316
Total other debt	31,735	30,365
Other liabilities	9,428	9,817
Total liabilities	256,184	255,301
Commitments, contingencies and guarantees (see Note 14)		
Stockholders' equity:		
Preferred stock (par value \$.01 per share; 50,000,000 shares authorized; 1,375,000 and 875,000 shares issued and outstanding as of September 30, 2014, and December 31, 2013, respectively)	0	0
	6	6

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Common stock (par value \$.01 per share; 1,000,000,000 shares authorized; 642,517,260 and 637,151,800 shares issued as of September 30, 2014, and December 31, 2013, respectively, and 558,526,922 and 572,675,375 shares outstanding as of September 30, 2014, and December 31, 2013, respectively)			
Additional paid-in capital, net	27,272		26,526
Retained earnings	23,162		20,292
Accumulated other comprehensive income	(559	)	(872)
Treasury stock at cost (par value \$.01 per share; 83,990,338 and 64,476,425 shares as of September 30, 2014, and December 31, 2013, respectively)	(5,863	)	(4,320)
Total stockholders' equity	44,018		41,632
Total liabilities and stockholders' equity	\$ 300,202		\$ 296,933
See Notes to Consolidated Financial Statements.			

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CAPITAL ONE FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)

(Dollars in millions, except per share data)	Preferred Stock		Common Stock			Additional Paid-In Capital	Retained Earnings ⁽¹⁾	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
	Shares	Amount	Shares	Amount	Amount					
Balance as of December 31, 2013	875,000	\$0	637,151,800	\$6	\$26,526	\$20,292	\$(872)	\$(4,320)	\$41,632	
Comprehensive income						3,429	313		3,742	
Cash dividends—common stock \$0.90 per share						(513)			(513)	
Cash dividends - preferred series B stock 6%, series C stock 6.25% per annum						(46)			(46)	
Purchases of treasury stock								(1,543)	(1,543)	
Issuances of common stock and restricted stock, net of forfeitures			1,078,458	0	73				73	
Exercise of stock options and warrants, tax benefits of exercises and restricted stock vesting			4,287,002	0	89				89	
Issuances of preferred stock (Series C)	500,000	0			484				484	
Compensation expense for restricted stock awards and stock options					100				100	
Balance as of September 30, 2014	1,375,000	\$0	642,517,260	\$6	\$27,272	\$23,162	\$(559)	\$(5,863)	\$44,018	

Retained earnings as of December 31, 2013 includes the cumulative impact of \$112 million resulting from the (1) adoption of ASU 2014-01 "Accounting For Investments in Qualified Affordable Housing Projects." See "Note 1—Summary of Significant Accounting Policies" for additional information.

See Notes to Consolidated Financial Statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Dollars in millions)	Nine Months Ended	
	September 30,	
	2014	2013
Operating activities:		
Income from continuing operations, net of tax	\$3,453	\$3,479
Loss from discontinued operations, net of tax	(24)	(210)
Net income	3,429	3,269
Adjustments to reconcile net income to cash provided by operating activities:		
Provision for credit losses	2,432	2,496
Depreciation and amortization, net	1,532	1,647
Net gain on sales of securities available for sale	(18)	(3)
Impairment losses on securities available for sale	15	40
Loans held for sale:		
Originations and purchases	(3,355)	(972)
Gain on sales	(35)	(23)
Proceeds from sales and paydowns	3,171	995
Stock plan compensation expense	167	172
Changes in operating assets and liabilities:		
Decrease in interest receivable	150	390
Decrease in other assets	607	1,191
Decrease in interest payable	(58)	(174)
Decrease in other liabilities	(375)	(298)
Net cash provided (used) by discontinued operations	39	(291)
Net cash provided by operating activities	7,701	8,439
Investing activities:		
Purchases of securities	(14,078)	(13,084)
Proceeds from paydowns and maturities of securities	6,717	11,785
Proceeds from sales of securities	6,827	1,355
Net (increase) decrease in loans held for investment	(8,351)	9,119
Principal recoveries of loans previously charged off	1,203	1,204
Purchases of premises and equipment	(405)	(622)
Net cash provided (used) by investing activities	(8,087)	9,757
Financing activities:		
Decrease in restricted cash for securitization investors	469	38
Net decrease in deposits	(265)	(5,662)
Issuance of securitized debt obligations	2,995	1,450
Maturities and paydowns of securitized debt obligations	(2,808)	(3,304)
Issuance of senior and subordinated notes and junior subordinated debentures	7,713	934
Redemption of junior subordinated debentures	0	(3,641)
Maturities and redemptions of senior and subordinate notes	(2,375)	(500)
Net decrease in other borrowings	(4,030)	(12,279)
Net proceeds from issuances of common stock	73	64
Net proceeds from issuances of preferred stock	484	0
Proceeds from share-based payment activities	89	73
Dividends paid on common stock	(513)	(383)
Dividends paid on preferred stock	(46)	(39)

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Purchases of treasury stock	(1,543)	(287)
Net cash provided (used) by financing activities	243		(23,536)
Decrease in cash and cash equivalents	(143	)	(5,340)
Cash and cash equivalents at beginning of the period	6,291		11,058	
Cash and cash equivalents at end of the period	\$6,148		\$5,718	
Supplemental cash flow information:				
Non-cash items:				
Net transfers from loans held for investment to loans held for sale	\$38		\$6,808	
Net debt exchange of senior and subordinated notes	0		1,968	
Interest paid	1,248		1,550	
Income tax paid	1,109		1,250	
See Notes to Consolidated Financial Statements.				

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CAPITAL ONE FINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company

Capital One Financial Corporation, a Delaware Corporation established in 1994 and headquartered in McLean, Virginia, is a diversified financial services holding company with banking and non-banking subsidiaries. Capital One Financial Corporation and its subsidiaries (the “Company”) offers a broad array of financial products and services to consumers, small businesses and commercial clients through branches, the internet and other distribution channels. As of September 30, 2014, our principal subsidiaries included:

• Capital One Bank (USA), National Association (“COBNA”), which offers credit and debit card products, other lending products and deposit products; and

• Capital One, National Association (“CONA”), which offers a broad spectrum of banking products and financial services to consumers, small businesses and commercial clients.

The Company and its subsidiaries are hereafter collectively referred to as “we,” “us” or “our.” COBNA and CONA are collectively referred to as the “Banks.”

We also offer products outside of the United States principally through Capital One (Europe) plc (“COEP”), an indirect subsidiary of COBNA organized and located in the U.K., and through a branch of COBNA in Canada. COEP has authority, among other things, to provide credit card loans. Our branch of COBNA in Canada also has the authority to provide credit card loans.

Our principal operations are currently organized for management reporting purposes into three primary business segments, which are defined primarily based on the products and services provided or the type of customer served: Credit Card, Consumer Banking and Commercial Banking. We provide details on our business segments, the integration of recent acquisitions into our business segments, and the allocation methodologies and accounting policies used to derive our business segment results in “Note 13—Business Segments.”

Basis of Presentation and Use of Estimates

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the U.S. (“U.S. GAAP”). The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported on the consolidated financial statements and related disclosures. These estimates are based on information available as of the date of the consolidated financial statements. While management makes its best judgment, actual amounts or results could differ from these estimates. Certain prior period amounts have been reclassified to conform to the current period presentation.

Principles of Consolidation

The consolidated financial statements include the accounts of Capital One Financial Corporation and all other entities in which we have a controlling financial interest. We determine whether we have a controlling financial interest in an entity by first evaluating whether the entity is a voting interest entity or a Variable Interest Entity (“VIE”). All significant intercompany account balances and transactions have been eliminated.

New Accounting Standards Adopted

Accounting for Investments in Qualified Affordable Housing Projects

In January 2014, the Financial Accounting Standard Board (“FASB”) issued guidance permitting an entity to account for Investments in Qualified Affordable Housing Projects using the proportional amortization method if certain criteria are met. The proportional amortization method amortizes the cost of the investment over the period in which the investor expects to receive tax credits and other tax benefits, and the resulting amortization is recognized as a component of income tax expense attributable to continuing operations. Historically, these investments were under the equity method of accounting and the passive losses related to the investments were recognized within non-interest expense. We adopted this guidance in the first quarter of 2014 with retrospective application. As a result, total assets, total liabilities, and retained earnings were reduced by \$115 million, \$3 million and \$112 million from \$297.0 billion, \$255.3 billion and \$20.4 billion, respectively, as of December 31, 2013. In addition, net income was reduced by \$12

million from \$1.1 billion for the three months ended September 30, 2013, and by \$31 million from \$3.3 billion for the first nine months ended September 30, 2013.

During the third quarter and first nine months of 2014, we recognized amortization of \$87 million and \$231 million, respectively, and tax credits of \$90 million and \$268 million, respectively, associated with these investments within income taxes. The carrying value of our investments in these qualified affordable housing projects was \$3.0 billion and \$2.8 billion as of September 30, 2014 and December 31, 2013, respectively. We are periodically required to provide additional financial or other support during the period of the investments. We recorded a liability of \$1.2 billion for the unfunded commitments as of September 30, 2014, which is expected to be paid from 2014 to 2017.

Obligations Resulting from Joint and Several Liability Arrangements

In February 2013, the FASB issued guidance for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation, within the scope of this guidance, is fixed at the reporting date, except for obligations addressed within existing guidance in U.S. GAAP. The guidance clarifies that an entity shall measure the obligations as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The guidance also requires an entity to disclose the nature and amounts of the obligations as well as other information about those obligations. The guidance is effective for annual and interim periods beginning after December 15, 2013. The adoption of this guidance in the first quarter of 2014 did not have a significant impact on our financial condition, results of operations or liquidity as the guidance is consistent with our current practice.

Recently Issued but Not Yet Adopted Accounting Standards

Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period

In June 2014, the FASB issued guidance clarifying that a performance target contained within a share-based payment award that affects vesting and can be achieved after the requisite service period has been completed is to be accounted for as a performance condition. Accordingly, the grantor of such awards would recognize compensation cost in the period in which it becomes probable that the performance target will be achieved. The amount of the compensation cost recognized should represent the cost attributable to the requisite service period fulfilled. The guidance is effective for annual and interim periods beginning after December 15, 2015, with early adoption permitted. Entities may elect to adopt the guidance on either a prospective or modified retrospective basis. We do not expect our adoption of this guidance in the first quarter of 2015 to have a significant impact on our financial condition, results of operations or liquidity as the guidance is consistent with our current practice.

Accounting for Repurchase Transactions

In June 2014, the FASB issued guidance that requires repurchase-to-maturity transactions to be accounted for as secured borrowings rather than sales. New disclosures will also be required for certain transactions accounted for as secured borrowings and transfers accounted for as sales when the transferor retains substantially all of the exposure to the economic return on the transferred financial assets. We do not expect our adoption of the accounting guidance in the first quarter of 2015 to have a significant impact on our financial condition, results of operations or liquidity as the guidance is consistent with our current practice. The new disclosures will be provided beginning in the second quarter of 2015.

Revenue from Contracts with Customers

In May 2014, the FASB issued revised guidance for the recognition, measurement, and disclosure of revenue from contracts with customers. The guidance is applicable to all entities and, once effective, will replace significant portions of existing industry and transaction-specific revenue recognition rules with a more principles-based recognition model. Most revenue associated with financial instruments, including interest and loan origination fees, is outside the scope of the guidance. Gains and losses on investment securities, derivatives and sales of financial instruments are similarly excluded from the scope. The guidance is effective for annual and interim periods beginning after December 15, 2016, with early adoption prohibited. Entities can elect to adopt the guidance either on a full or modified retrospective basis. Full retrospective adoption will require a cumulative effect adjustment to retained earnings as of the beginning of the earliest comparative period presented. Modified retrospective adoption will require a cumulative effect adjustment to retained earnings as of the beginning of the reporting period in which the entity first applies the new guidance. We are currently evaluating the guidance to identify which of our revenue streams are

within its scope and determine which transition method we plan to elect. Accordingly, we cannot yet quantify the impact our adoption of this guidance will have in the first quarter of 2017.

Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity

In April 2014, the FASB issued guidance changing the criteria for reporting discontinued operations. As a result of the change, only those disposals of components of an entity that represent a strategic shift that have, or will have, a major effect on an entity's operations and financial results will be reported as discontinued operations. Expanded disclosures will be required of discontinued operations and disposals of individually significant components of an entity that do not currently qualify for discontinued operations reporting. The guidance is effective for disposals or classifications as held for sale of components of an entity that occur within annual and interim periods beginning after December 15, 2014, with early adoption permitted in certain circumstances. Our adoption of this guidance in the first quarter of 2015 will not impact what we currently report as discontinued operations due to the prospective transition provisions.

Reclassification of Collateralized Mortgage Loans Upon Foreclosure

In January 2014, the FASB issued guidance clarifying when an entity should reclassify a consumer mortgage loan collateralized by residential real estate to foreclosed property. Reclassification should occur when the creditor obtains legal title to the residential real estate property or when the borrower conveys all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. An entity should not wait until a redemption period, if any, has expired to reclassify a consumer mortgage loan to foreclosed property. The guidance is effective for annual and interim periods beginning after December 15, 2014, with early adoption permitted. We do not expect our adoption of this guidance in the first quarter of 2015 to have a significant impact on our financial condition, results of operations or liquidity as the guidance is materially consistent with our current practice.

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CAPITAL ONE FINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 2—DISCONTINUED OPERATIONS

Shutdown of Mortgage Origination Operations of our Wholesale Mortgage Banking Unit

In the third quarter of 2007, we closed the mortgage origination operations of our wholesale mortgage banking unit, GreenPoint Mortgage Funding Inc. (“GreenPoint”), which we acquired in December 2006 as part of the North Fork acquisition. The results of the wholesale banking unit have been accounted for as a discontinued operation and are therefore not included in our results from continuing operations for the three and nine months ended September 30, 2014 and 2013. We have no significant continuing involvement in these operations.

The following table summarizes the results from discontinued operations related to the closure of the mortgage origination operations of our wholesale mortgage banking unit:

Table 2.1: Results of Discontinued Operations

(Dollars in millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Non-interest expense, net	\$(70)	\$(20)	\$(38)	\$(335)
Loss from discontinued operations before income taxes	(70)	(20)	(38)	(335)
Income tax benefit	(26)	(7)	(14)	(125)
Loss from discontinued operations	\$(44)	\$(13)	\$(24)	\$(210)

The discontinued mortgage origination operations of our wholesale mortgage banking unit has remaining assets of \$353 million and \$370 million as of September 30, 2014 and December 31, 2013, respectively, which primarily consisted of the deferred tax asset related to the reserve for representations and warranties. Liabilities, which primarily consisted of reserves for representations and warranties repurchases on loans previously sold to third parties, totaled \$982 million and \$960 million as of September 30, 2014 and December 31, 2013, respectively.

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CAPITAL ONE FINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 3—INVESTMENT SECURITIES

Our investment portfolio consists primarily of the following: U.S. Treasury debt; U.S. agency debt and corporate debt securities guaranteed by U.S. government agencies; U.S. government sponsored enterprise or agency (“Agency”) and non-agency residential mortgage-backed securities (“RMBS”) and commercial mortgage-backed securities (“CMBS”); other asset-backed securities (“ABS”); and other investments. The carrying value of our investments in U.S. Treasury, Agency securities and other securities guaranteed by the U.S. government or U.S. government agencies represents 85% and 77% of our total investment securities as of September 30, 2014 and December 31, 2013, respectively.

Our investment portfolio includes securities available for sale and securities held to maturity. We classify securities as available for sale or held to maturity based on our investment strategy and management’s assessment of our intent and ability to hold the securities until maturity.

The table below presents the overview of our investment portfolio at September 30, 2014 and December 31, 2013.

Table 3.1: Overview of Investment Portfolio

(Dollars in millions)	September 30, 2014	December 31, 2013
Securities available for sale, at fair value	\$ 39,665	\$ 41,800
Securities held to maturity, at carrying value	22,182	19,132
Total investments	\$ 61,847	\$ 60,932

The table below presents the amortized cost, gross unrealized gains and losses, and fair value of securities available for sale at September 30, 2014 and December 31, 2013.

Table 3.2: Investment Securities Available for Sale

(Dollars in millions)	September 30, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses ⁽¹⁾	Fair Value
Investment securities available for sale:				
U.S. Treasury debt obligations	\$4,261	\$2	\$(2)	\$4,261
U.S. agency debt obligations	1	0	0	1
Corporate debt securities guaranteed by U.S. government agencies	1,001	1	(23)	979
Residential mortgage-backed securities (“RMBS”):				
Agency ⁽²⁾	20,853	274	(141)	20,986
Non-agency	3,024	486	(13)	3,497
Total RMBS	23,877	760	(154)	24,483
Commercial mortgage-backed securities (“CMBS”):				
Agency ⁽²⁾	4,029	25	(71)	3,983
Non-agency	1,809	22	(28)	1,803
Total CMBS	5,838	47	(99)	5,786
Other asset-backed securities (“ABS” ⁽³⁾)	3,038	58	(13)	3,083
Other securities ⁽⁴⁾	1,087	6	(21)	1,072
Total investment securities available for sale	\$39,103	\$874	\$(312)	\$39,665

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(Dollars in millions)	December 31, 2013			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses ⁽¹⁾	
Investment securities available for sale:				