KEYCORP /NEW/
Form 10-Q
November 01, 2017
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, 2017

Commission File Number 001-11302

Exact name of registrant as specified in its charter:

Ohio	34-6542451
State or other jurisdiction of incorporation or organization:	I.R.S. Employer Identification Number:

127 Public Square, Cleveland, Ohio	44114-1306
Address of principal executive offices:	Zip Code:

(216) 689-3000
Registrant's telephone number, including area code:

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

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

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
Emerging growth company		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

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

Common Shares with a par value of $1 each	1,075,399,655 shares
Title of class	Outstanding at October 30, 2017

Table of Contents

KEYCORP
TABLE OF CONTENTS
PART I. FINANCIAL INFORMATION

Table of Contents

Table of Contents

PART I. FINANCIAL INFORMATION

Item 2. Management’s Discussion & Analysis of Financial Condition & Results of Operations

Introduction

This section reviews the financial condition and results of operations of KeyCorp and its subsidiaries for the quarterly periods ended September 30, 2017, and September 30, 2016. Some tables may include additional periods to comply with disclosure requirements or to illustrate trends in greater depth. When you read this discussion, you should also refer to the consolidated financial statements and related notes in this report. The page locations of specific sections and notes that we refer to are presented in the Table of Contents.

References to our “2016 Form 10-K” refer to our Form 10-K for the year ended December 31, 2016, which has been filed with the SEC and is available on its website (www.sec.gov) and on our website (www.key.com/ir).

Terminology

Throughout this discussion, references to “Key,” “we,” “our,” “us,” and similar terms refer to the consolidated entity consisting of KeyCorp and its subsidiaries. “KeyCorp” refers solely to the parent holding company, and “KeyBank” refers to KeyCorp’s subsidiary bank, KeyBank National Association.

Throughout the following discussion, industry-specific terms are used as defined below:

- We use the phrase continuing operations in this document to mean all of our businesses other than the education lending business and Austin. The education lending business and Austin have been accounted for as discontinued operations since 2009.
- Our exit loan portfolios are separate from our discontinued operations. These portfolios, which are in a run-off mode, stem from product lines we decided to cease because they no longer fit with our corporate strategy. These exit loan portfolios are included in Other Segments.
- We engage in capital markets activities primarily through business conducted by our Key Corporate Bank segment. These activities encompass a variety of products and services. Among other things, we trade securities as a dealer, enter into derivative contracts (both to accommodate clients’ financing needs and to mitigate certain risks), and conduct transactions in foreign currencies (both to accommodate clients’ needs and to benefit from fluctuations in exchange rates).
- For regulatory purposes, capital is divided into two classes. Federal regulations currently prescribe that at least one-half of a bank or BHC’s total risk-based capital must qualify as Tier 1 capital. Both total and Tier 1 capital serve as bases for several measures of capital adequacy, which is an important indicator of financial stability and condition. As described under the heading “Regulatory capital requirements – Capital planning and stress testing” in the section entitled “Supervision and Regulation” that begins on page 8 of our 2016 Form 10-K, the regulators are required to conduct a supervisory capital assessment of all BHCs with assets of at least $50 billion, including KeyCorp. As part of this capital adequacy review, banking regulators evaluate a component of Tier 1 capital, known as Common Equity Tier 1, under the Regulatory Capital Rules. The “Capital” section of this report under the heading “Capital adequacy” provides more information on total capital, Tier 1 capital, and the Regulatory Capital Rules, including Common Equity Tier 1, and describes how these measures are calculated.

Table of Contents

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

AICPA: American Institute of Certified Public Accountants.
ALCO: Asset/Liability Management Committee.
ALLL: Allowance for loan and lease losses.
A/LM: Asset/liability management.
AOCI: Accumulated other comprehensive income (loss).
APBO: Accumulated postretirement benefit obligation.
Austin: Austin Capital Management, Ltd.
BHCs: Bank holding companies.
Board: KeyCorp Board of Directors.
CCAR: Comprehensive Capital Analysis and Review.
CMBS: Commercial mortgage-backed securities.
CME: Chicago Mercantile Exchange.
CMO: Collateralized mortgage obligation.
Common Shares: KeyCorp common shares, $1 par value.
DIF: Deposit Insurance Fund of the FDIC.
Dodd-Frank Act: Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.
EBITDA: Earnings before interest, taxes, depreciation, and amortization.
EPS: Earnings per share.
ERISA: Employee Retirement Income Security Act of 1974.
ERM: Enterprise risk management.
EVE: Economic value of equity.
FASB: Financial Accounting Standards Board.
FDIC: Federal Deposit Insurance Corporation.
Federal Reserve: Board of Governors of the Federal Reserve System.
FHLB: Federal Home Loan Bank of Cincinnati.
FHLMC: Federal Home Loan Mortgage Corporation.
FICO: Fair Isaac Corporation
First Niagara: First Niagara Financial Group, Inc. (NASDAQ: FNFG).
FNMA: Federal National Mortgage Association, or Fannie Mae.
FSOC: Financial Stability Oversight Council.
GAAP: U.S. generally accepted accounting principles.
GNMA: Government National Mortgage Association, or Ginnie Mae.
HelloWallet: HelloWallet, LLC.
ISDA: International Swaps and Derivatives Association.
KAHC: Key Affordable Housing Corporation.
KBCM: KeyBanc Capital Markets, Inc.
KCC: Key Capital Corporation.
KCDC: Key Community Development Corporation.
KEF: Key Equipment Finance.
KPP: Key Principal Partners.
KREEC: Key Real Estate Equity Capital, Inc.
LCR: Liquidity coverage ratio.
LIBOR: London Interbank Offered Rate.
LIHTC: Low-income housing tax credit.
LTV: Loan-to-value.
Moody's: Moody's Investor Services, Inc.
MRM: Market Risk Management group.
N/A: Not applicable.
NASDAQ: The NASDAQ Stock Market LLC.
NAV: Net asset value.
N/M: Not meaningful.
NOW: Negotiable Order of Withdrawal.
NPR: Notice of proposed rulemaking.
NYSE: New York Stock Exchange.
OCC: Office of the Comptroller of the Currency.
OCI: Other comprehensive income (loss).
OREO: Other real estate owned.
OTTI: Other-than-temporary impairment.
PBO: Projected benefit obligation.
PCI: Purchased credit impaired.
S&P: Standard and Poor's Ratings Services, a Division of The McGraw-Hill Companies, Inc.
SEC: U.S. Securities and Exchange Commission.
Series A Preferred Stock: KeyCorp's 7.750% Noncumulative Perpetual Convertible Preferred Stock, Series A.
SIFIs: Systemically important financial institutions including BHCs with total consolidated assets of at least $50 billion and nonbank financial companies designated by FSOC for supervision by the Federal Reserve.
TDR: Troubled debt restructuring.
TE: Taxable-equivalent.
U.S. Treasury: United States Department of the Treasury.
VaR: Value at risk.
VEBA: Voluntary Employee Beneficiary Association.
VIE: Variable interest entity.

Table of Contents

Forward-looking statements

From time to time, we have made or will make forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements do not relate strictly to historical or current facts. Forward-looking statements usually can be identified by the use of words such as "goal," "objective," "plan," "expect," "assume," "anticipate," "intend," "project," "believe," "estimate," or other words of similar meaning. Forward-looking stateme provide our current expectations or forecasts of future events, circumstances, results or aspirations. Our disclosures in this report contain forward-looking statements. We may also make forward-looking statements in other documents filed with or furnished to the SEC. In addition, we may make forward-looking statements orally to analysts, investors, representatives of the media, and others.

Forward-looking statements, by their nature, are subject to assumptions, risks, and uncertainties, many of which are outside of our control. Our actual results may differ materially from those set forth in our forward-looking statements. There is no assurance that any list of risks and uncertainties or risk factors is complete. Factors that could cause our actual results to differ from those described in forward-looking statements include, but are not limited to:

- deterioration of commercial real estate market fundamentals;
- defaults by our loan counterparties or clients;
- adverse changes in credit quality trends;
- declining asset prices;
- our concentrated credit exposure in commercial and industrial loans;
- the extensive and increasing regulation of the U.S. financial services industry;
- operational or risk management failures by us or critical third parties;
- changes in accounting policies, standards, and interpretations;
- breaches of security or failures of our technology systems due to technological or other factors and cybersecurity threats;
- negative outcomes from claims or litigation;
- the occurrence of natural or man-made disasters, conflicts, or terrorist attacks, or other adverse external events;
- evolving capital and liquidity standards under applicable regulatory rules;
- unanticipated changes in our liquidity position, including but not limited to, changes in our access to or the cost of funding and our ability to secure alternative funding sources;
- downgrades in our credit ratings or those of KeyBank;
- a reversal of the U.S. economic recovery due to financial, political, or other shocks;
- our ability to anticipate interest rate changes and manage interest rate risk;
- deterioration of economic conditions in the geographic regions where we operate;
- the soundness of other financial institutions;
- tax reform and other changes in tax laws;
- our ability to attract and retain talented executives and employees and to manage our reputational risks;
- our ability to timely and effectively implement our strategic initiatives;
- increased competitive pressure due to industry consolidation;
- our ability to adapt our products and services to industry standards and consumer preferences;
- unanticipated adverse effects of strategic partnerships or acquisitions and dispositions of assets or businesses;
- our ability to realize the anticipated benefits of the First Niagara merger; and
- our ability to develop and effectively use the quantitative models we rely upon in our business planning.

Any forward-looking statements made by us or on our behalf speak only as of the date they are made, and we do not undertake any obligation to update any forward-looking statement to reflect the impact of subsequent events or circumstances. Before making an investment decision, you should carefully consider all risks and uncertainties disclosed in our SEC filings, including this report on Form 10-Q and our subsequent reports on Forms 8-K, 10-Q, and 10-K, and our registration statements under the Securities Act of 1933, as amended, all of which are or will upon filing be accessible on the SEC's website at www.sec.gov and on our website at www.key.com/ir.

Table of Contents

Selected financial data

Our financial performance for each of the last five quarters is summarized in Figure 1.

Figure 1. Selected Financial Data

	2017			2016		Nine months ended September 30,	
dollars in millions, except per share amounts	Third	Second	First	Fourth	Third	2017	2016
FOR THE PERIOD							
Interest income	$1,109	$1,117	$1,050	$1,062	$890	$3,276	$2,257
Interest expense	161	144	132	124	110	437	276
Net interest income	948	973	918	938	780	2,839	1,981
Provision for credit losses	51	66	63	66	59	180	200
Noninterest income	592	653	577	618	549	1,822	1,453
Noninterest expense	992	995	1,013	1,220	1,082	3,000	2,536
Income (loss) from continuing operations before income taxes	497	565	419	270	188	1,481	698
Income (loss) from continuing operations attributable to Key	363	407	324	233	171	1,094	557
Income (loss) from discontinued operations, net of taxes [(a)]	1	5	—	(4)	1	6	5
Net income (loss) attributable to Key	364	412	324	229	172	1,100	562
Income (loss) from continuing operations attributable to Key common shareholders	349	393	296	213	165	1,038	540
Income (loss) from discontinued operations, net of taxes [(a)]	1	5	—	(4)	1	6	5
Net income (loss) attributable to Key common shareholders	350	398	296	209	166	1,044	545
PER COMMON SHARE							
Income (loss) from continuing operations attributable to Key common shareholders	$.32	$.36	$.28	$.20	$.17	$.96	$.61
Income (loss) from discontinued operations, net of taxes [(a)]	—	—	—	—	—	.01	.01
Net income (loss) attributable to Key common shareholders [(b)]	.32	.37	.28	.20	.17	.97	.62
Income (loss) from continuing operations attributable to Key common shareholders — assuming dilution	.32	.36	.27	.20	.16	.95	.60
Income (loss) from discontinued operations, net of taxes — assuming dilution [(a)]	—	—	—	—	—	.01	.01
Net income (loss) attributable to Key common shareholders — assuming dilution [(b)]	.32	.36	.27	.19	.17	.96	.61
Cash dividends paid	.095	.095	.085	.085	.085	.275	.245

Book value at period end	13.18	13.02	12.71	12.58	12.78	13.18	12.78
Tangible book value at period end	10.52	10.40	10.21	9.99	10.14	10.52	10.14
Market price:							
High	19.37	19.10	19.53	18.62	12.64	19.37	13.37
Low	16.47	16.91	16.54	12.00	10.38	16.47	9.88
Close	18.82	18.74	17.78	18.27	12.17	18.82	12.17
Weighted-average common shares outstanding (000)	1,073,390	1,076,203	1,068,609	1,067,771	982,080	1,075,296	880,824
Weighted-average common shares and potential common shares outstanding (000) [c]	1,088,841	1,093,039	1,086,540	1,083,717	994,660	1,091,655	889,789
AT PERIOD END							
Loans	$86,492	$86,503	$86,125	$86,038	$85,528	$86,492	$85,528
Earning assets	122,625	121,243	120,261	121,966	121,089	122,625	121,089
Total assets	136,733	135,824	134,476	136,453	135,805	136,733	135,805
Deposits	103,446	102,821	103,982	104,087	104,185	103,446	104,185
Long-term debt	15,100	13,261	12,324	12,384	12,622	15,100	12,622
Key common shareholders’ equity	14,224	14,228	13,951	13,575	13,831	14,224	13,831
Key shareholders’ equity	15,249	15,253	14,976	15,240	14,996	15,249	14,996
PERFORMANCE RATIOS — FROM CONTINUING OPERATIONS							
Return on average total assets	1.07 %	1.23 %	.99 %	.69 %	.55 %	1.10 %	.71 %
Return on average common equity	9.74	11.12	8.76	6.22	5.09	9.89	6.28
Return on average tangible common equity [d]	12.21	13.80	10.98	7.88	6.16	12.36	7.21
Net interest margin (TE)	3.15	3.30	3.13	3.12	2.85	3.19	2.84
Cash efficiency ratio [d]	62.2	59.3	65.8	76.2	80.0	62.4	72.5
PERFORMANCE RATIOS — FROM CONSOLIDATED OPERATIONS							
Return on average total assets	1.06 %	1.23 %	.98 %	.67 %	.55 %	1.09 %	.70 %
Return on average common equity	9.77	11.26	8.76	6.10	5.12	9.95	6.34
Return on average tangible common equity [d]	12.25	13.98	10.98	7.73	6.20	12.43	7.27
Net interest margin (TE)	3.13	3.28	3.11	3.09	2.83	3.17	2.81
Loan-to-deposit [e]	86.2	87.2	85.6	85.2	84.7	86.2	84.7
CAPITAL RATIOS AT PERIOD END							
Key shareholders’ equity to assets	11.15 %	11.23 %	11.14 %	11.17 %	11.04 %	11.15 %	11.04 %
Key common shareholders’ equity to assets	10.40	10.48	10.37	9.95	10.18	10.40	10.18
Tangible common equity to tangible assets [d]	8.49	8.56	8.51	8.09	8.27	8.49	8.27
Common Equity Tier 1	10.26	9.91	9.91	9.54	9.56	10.26	9.56
Tier 1 risk-based capital	11.11	10.73	10.74	10.89	10.53	11.11	10.53
Total risk-based capital	13.09	12.64	12.69	12.85	12.63	13.09	12.63
Leverage	9.83	9.95	9.81	9.90	10.22	9.83	10.22
TRUST ASSETS							
Assets under management	$38,660	$37,613	$37,417	$36,592	$36,752	$38,660	$36,752
OTHER DATA							
Average full-time-equivalent employees	18,548	18,344	18,386	18,849	17,079	18,427	14,642
Branches	1,208	1,210	1,216	1,217	1,322	1,208	1,322

(a)

In April 2009, management decided to wind down the operations of Austin Capital Management, Ltd., a subsidiary that specialized in managing hedge fund investments for institutional customers. In September 2009, management decided to discontinue the education lending business conducted through Key Education

7

Table of Contents

Resources, the education payment and financing unit of KeyBank. As a result of this decision, we have accounted for this business as a discontinued operation. For further discussion regarding the income (loss) from discontinued operations, see Note 12 (“Acquisition, Divestiture, and Discontinued Operations”).
(b) EPS may not foot due to rounding.
(c) Assumes conversion of Common Share options and other stock awards and/or convertible preferred stock, as applicable.
(d) See Figure 6 entitled “GAAP to Non-GAAP Reconciliations,” which presents the computations of certain financial measures related to “tangible common equity” and “cash efficiency.” The table reconciles the GAAP performance measures to the corresponding non-GAAP measures, which provides a basis for period-to-period comparisons.
(e) Represents period-end consolidated total loans and loans held for sale divided by period-end consolidated total deposits.

Economic Overview

The initial estimate of third quarter 2017 GDP came in at 3.0%, building on the strong growth experienced during the second quarter of 2017 of 3.1%. Personal consumption expenditures, the economy’s largest component, contributed 1.6% to growth in the third quarter, somewhat behind 2.2% contributed in the second quarter of 2017 but still ahead of the1.3% contributed in the first quarter of 2017. Inventories had a sizable impact on third quarter 2017 growth, accounting for .7%, possibly indicating that businesses are anticipating increased demand in the near future. A shrinking trade deficit also helped to lift the third quarter 2017 figure, adding .4% to the total. Unfortunately, many forecasts are expecting this third quarter 2017 GDP figure to be revised lower in coming months, once economists are able to more accurately assess the economic damage caused by hurricanes Harvey, Irma, and Maria.

The International Monetary Fund estimates that global growth is expected to rise from 3.1% in 2016 to 3.6% in 2017 and 3.7% in 2018 with broad-based upward revisions in the European area, Japan, emerging markets in Asia, emerging markets in Europe, and Russia more than offsetting downward revisions for the United States and the United Kingdom.

Oil prices have fallen since the beginning of the year to $52 per barrel, but are well above the lows in early 2016 when prices dropped to $25 per barrel. Although inventories remain elevated, recent declines may help clear the way for stronger appreciation in the coming quarters and help support America’s struggling energy industry.

The stock market continues to reach new records, with the S&P 500 equity index up 12.5% since the end of 2016. A general rally has occurred following the November 2016 elections, and based on expectations for growth-friendly economic policies from the new U.S. presidential administration.

274,000 new jobs were added in the U.S. during the third quarter of 2017. This was down from the second quarter of 2017, which saw gains of 562,000. Hurricanes Harvey and Irma distorted the employment situation in September when payroll employment declined by 33,000 jobs. Leisure and hospitality created most of the drag, declining by 111,000 jobs. The unemployment rate declined to 4.2%, but this was likely because of the inability to access all of the sample households in storm affected areas. Based on the experience of previous hurricanes, the September 2017 numbers are likely to undergo dramatic revisions. Still, the participation rate increased to 63.1%, a welcome development. This was the first time it rose above 63% since early 2014. The number of unemployed declined, the employment-to-population ratio increased, the number of discouraged workers fell, and fewer workers were employed part time involuntarily. Year-over-year earnings growth came in at 2.9%, above the recent range of around 2.5%. However, the boost may be attributed in part to an outsized decline in the lowest-paying jobs.

Headline inflation was up by 2.2% year over year at the end of the third quarter of 2017, slightly above the Federal Reserve’s target of 2.0%. However core inflation, excluding food and energy, was subdued year over year, at 1.7%.

Thanks to the solid economy and still low interest rates, the housing market generally benefited in the third quarter of 2017. New home sales were down 2.1% compared to the third quarter of 2016, while existing home sales were slightly up .4% compared to third quarter 2016 levels. However, prices are up uniformly, with average new home prices up 3.4% from year ago levels, and existing home prices up 5.1%. Single family housing starts also posted respectable gains in the third quarter of 2017, up 12.7%, from the third quarter of 2016. Multi-family construction was down 5.2%.

The Federal Open Market Committee left the federal funds rate unchanged in September 2017 at 1% to 1.25%. The minutes from the September meeting showed a debate on the weakness in inflation, and whether it can be attributed to transitory or more persistent factors. The Federal Reserve (like many economists) is unsure why inflationary pressures haven't developed as slack in the broader economy has diminished. This uncertainty suggests that a December 2017 rate hike is not a sure thing, but most believe it is still likely. The minutes also discussed the economic cost of the recent hurricanes and how it will likely distort the incoming data on growth and

Table of Contents

inflation. However, the Federal Reserve doesn't expect the hurricanes to alter the course of the economy over the medium term. The 10-year U.S. Treasury yield stood at 2.33% at the end of the third quarter of 2017, which was only two basis points below the prior quarter.

Long-term financial targets

Our long-term financial targets are as follows:

- Generate positive operating leverage and a cash efficiency ratio of less than 60%;
- Maintain a moderate risk profile by targeting a net loan charge-offs to average loans ratio in the range of .40% to .60%; and
- Achieve a return on tangible common equity ratio in the range of 13% to 15%.

Figure 2 shows the evaluation of our long-term financial targets for the three months and nine months ended September 30, 2017.

Figure 2. Evaluation of Our Long-Term Targets

	Key Metrics [a]	3Q17		YTD 2017		Targets
Positive operating leverage	Cash efficiency ratio [b]	62.2	%	62.4	%	< 60%
	Cash efficiency ratio excluding notable items [b]	59.7	%	59.8	%	
Moderate Risk Profile	Net loan charge-offs to average loans	.15	%	.24	%	.40 - .60%
Financial Returns	Return on average tangible common equity [b]	12.21	%	12.36	%	13.00 - 15.00%
	Return on average tangible common equity excluding notable items [b]	13.19	%	12.98	%	

(a) Calculated from continuing operations, unless otherwise noted.
(b) Non-GAAP measure; see Figure 6 entitled "GAAP to Non-GAAP Reconciliations" for reconciliation.

Strategic developments

Our actions and results during the first nine months of 2017 supported our corporate strategy described in the "Introduction" section under the "Corporate strategy" heading on page 35 of our 2016 Form 10-K.

- We continued to generate positive operating leverage versus the prior year and our cash efficiency ratio improved to 62.4%, or 59.8%, excluding notable items. Revenue growth was driven by net interest income and fee-based businesses. Cards and payments had a record quarter, up 13.6% from the year-ago quarter, reflecting the investments we have made in the businesses, our recent merchant services acquisition and some of our early successes with First Niagara clients. Expenses remain well managed, with our quarterly results reflecting our recent acquisitions of HelloWallet and Key Merchant Services, LLC, as well as seasonal trends.
- Early in the fourth quarter of 2017, we completed the acquisition of Cain Brothers, a leading healthcare-focused merger and acquisitions investment bank. The move will significantly expand our existing healthcare vertical and further enhances our ability to serve our clients with distinctive expertise and capabilities.
- Net loan charge-offs were .24% of average loans for the first nine months of 2017, down from .27% for the same period one-year ago and below our targeted range. Total net loan charge-offs increased during the first nine months of 2017 compared to the year-ago period. Total loans charged off increased in our commercial and industrial loan portfolio and our auto loan portfolio which is included in our consumer indirect loan portfolio. Partially offsetting these increases in loan charge-offs were increases in recoveries in our commercial and industrial loan portfolio, driven by a large recovery that occurred during the third quarter of 2017.
- Capital management remains a priority for 2017. As previously reported, share repurchases of up to $800 million were included in the 2017 capital plan, which is effective through the second quarter of 2018. We completed $277

million of Common Share repurchases, including $271 million of Common Share repurchases in the open market and $6 million of Common Share repurchases related to employee equity compensation programs in the third quarter of 2017 under this authorization. Over the past five years, we have repurchased over $2 billion in common shares.

- Consistent with our 2016 capital plan, the Board declared a quarterly dividend of $.095 per Common Share for the third quarter of 2017. Potential dividend increases were also included in our 2017 capital plan. In the fourth quarter of 2017, the Board plans to consider a potential increase in our quarterly common share dividend, up to $.105 per share, consistent with the 2017 capital plan. An additional potential increase in the quarterly common share dividend, up to $.12 per share, is expected to be considered by the Board for the second quarter of 2018.

Table of Contents

Demographics

We have two major business segments: Key Community Bank and Key Corporate Bank. Key Community Bank serves individuals and small to mid-sized businesses by offering a variety of deposit and investment, lending, credit card, and personalized wealth management products and business advisory services. Key Community Bank offers personal property and casualty insurance, such as home, auto, renters, watercraft, and umbrella policies. Key Community Bank also purchases motor vehicle retail installment sales contracts relating to new or used automobiles and light and medium-duty trucks via a network of dealers who regularly originate these third party installment sales contracts. These products and services are provided primarily through our relationship managers and specialists working in our 15-state branch network, which is organized into ten internally defined geographic regions: Washington, Oregon/Alaska, Rocky Mountains, Indiana/Northwest Ohio/Michigan, Central/Southwest Ohio, East Ohio/Western Pennsylvania, Atlantic, Western New York, Eastern New York, and New England. In addition, some of these product capabilities are delivered by Key Corporate Bank to clients of Key Community Bank.

Key Corporate Bank is a full-service corporate and investment bank focused principally on serving the needs of middle market clients in seven industry sectors: consumer, energy, healthcare, industrial, public sector, real estate, and technology. Key Corporate Bank delivers a broad suite of banking and capital markets products to its clients, including syndicated finance, debt and equity capital markets, commercial payments, equipment finance, commercial mortgage banking, derivatives, foreign exchange, financial advisory, and public finance. Key Corporate Bank is also a significant servicer of commercial mortgage loans and a significant special servicer of CMBS. Key Corporate Bank delivers many of its product capabilities to clients of Key Community Bank.

Further information regarding the products and services offered by our Key Community Bank and Key Corporate Bank segments is included in this report in Note 19 (“Line of Business Results”).

Supervision and regulation

The following discussion provides a summary of recent regulatory developments and should be read in conjunction with the disclosure included in our 2016 Form 10-K under the heading “Supervision and Regulation” in Item 1. Business and under the heading “II. Compliance Risk” in Item 1A. Risk Factors.

Regulatory capital requirements

In July 2013, the U.S. banking agencies adopted a final rule to implement the Basel III international capital framework (“Basel III”) with an effective date of January 1, 2015, and a multi-year transition period ending on December 31, 2018 (“Regulatory Capital Rules”). Consistent with Basel III, the Regulatory Capital Rules further restrict the type of instruments that may be recognized in Tier 1 and Tier 2 capital (including the phase out of trust preferred securities from Tier 1 capital for BHCs above a certain asset threshold, like KeyCorp), establish a minimum Tier 1 Common Equity Capital ratio requirement of 4.5% and capital buffers to address procyclicality concerns and absorb losses during periods of financial stress, and refine several of the methodologies used for determining risk-weighted assets. The Regulatory Capital Rules provide additional requirements for large banking organizations with over $250 billion in total consolidated assets or $10 billion in foreign exposure, but those additional requirements do not apply to KeyCorp nor to KeyBank. Accordingly, for purposes of the Regulatory Capital Rules, KeyCorp and KeyBank are treated as “standardized approach” banking organizations.

The Basel III capital framework and the U.S. implementation of the Basel III capital framework are discussed in more detail in Item 1. Business of our 2016 Form 10-K under the heading “Supervision and Regulation - Regulatory capital requirements.”

Under the Regulatory Capital Rules, standardized approach banking organizations are required to meet the minimum capital and leverage ratios set forth in Figure 3 below. At September 30, 2017, Key had an estimated Common Equity Tier 1 Capital Ratio of 10.15% under the fully phased-in Regulatory Capital Rules. Also at September 30, 2017, based on the fully phased-in Regulatory Capital Rules, Key estimates that its capital and leverage ratios, after adjustment for market risk, would be as set forth in Figure 3.

Table of Contents

Figure 3. Pro Forma Ratios vs. Minimum Capital Ratios Calculated Under the Fully Phased-In Regulatory Capital Rules

Ratios (including capital conservation buffer)	Key September 30, 2017 Pro forma		Minimum January 1, 2017		Phase-in Period	Minimum January 1, 2019	
Common Equity Tier 1 [(a)]	10.15	%	4.5	%	None	4.5	%
Capital conservation buffer [(b)]			—		1/1/16-1/1/19	2.5	
Common Equity Tier 1 + Capital conservation buffer			4.5		1/1/16-1/1/19	7.0	
Tier 1 Capital	11.00	%	6.0		None	6.0	
Tier 1 Capital + Capital conservation buffer			6.0		1/1/16-1/1/19	8.5	
Total Capital	13.00	%	8.0		None	8.0	
Total Capital + Capital conservation buffer			8.0		1/1/16-1/1/19	10.5	
Leverage [(c)]	9.79	%	4.0		None	4.0	

(a) See Figure 6 entitled "GAAP to Non-GAAP Reconciliations," which presents the computation of Common Equity Tier 1 under the fully phased-in regulatory capital rules.

(b) Capital conservation buffer must consist of Common Equity Tier 1 capital. As a standardized approach banking organization, KeyCorp is not subject to the countercyclical capital buffer of up to 2.5% imposed upon an advanced approaches banking organization under the Regulatory Capital Rules.

(c) As a standardized approach banking organization, KeyCorp is not subject to the 3% supplemental leverage ratio requirement, which becomes effective January 1, 2018.

Revised prompt corrective action framework

The federal prompt corrective action ("PCA") framework under the FDIA groups FDIC-insured depository institutions into one of five capital categories: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized," for purposes of determining whether a bank should be required to establish a capital restoration plan and become subject to limitations on the bank's activities, capital actions, and payment of management fees.

In addition to implementing Basel III in the United States, the Regulatory Capital Rules also revised the capital category thresholds under the PCA framework for FDIC-insured depository institutions such as KeyBank. The revised PCA framework table in Figure 4 identifies the capital category thresholds for a "well capitalized" and an "adequately capitalized" institution under the Regulatory Capital Rules.

Figure 4. "Well Capitalized" and "Adequately Capitalized" Capital Category Ratios under Revised PCA Framework

Prompt Corrective Action	Capital Category			
Ratio	Well Capitalized [(a)]		Adequately Capitalized	
Common Equity Tier 1 Risk-Based	6.5	%	4.5	%
Tier 1 Risk-Based	8.0		6.0	
Total Risk-Based	10.0		8.0	
Tier 1 Leverage [(b)]	5.0		4.0	

(a) A "well capitalized" institution also must not be subject to any written agreement, order, or directive to meet and maintain a specific capital level for any capital measure.

(b) As a "standardized approach" banking organization, KeyBank is not subject to the 3% supplemental leverage ratio requirement, which becomes effective January 1, 2018.

We believe that, as of September 30, 2017, KeyBank (consolidated) satisfied the risk-based and leverage capital requirements to be considered “well capitalized” for purposes of the revised PCA framework. However, investors should not regard this determination as a representation of the overall financial condition or prospects of KeyBank because the PCA framework is intended to serve a limited supervisory function. Moreover, it is important to note that the PCA framework does not apply to BHCs, like KeyCorp.

Recent developments

On September 27, 2017, the federal banking agencies issued a joint proposal to simplify the Regulatory Capital Rules for standardized approach banking organizations (the “Simplification Proposal”), including Key. In anticipation of the Simplification Proposal, on August 22, 2017, the agencies issued a proposal to extend the current capital treatment for certain items that are subject to the multi-year transition period for the Regulatory Capital Rules, which ends on December 31, 2018. That proposal would alleviate the burden that could result from the

Table of Contents

continued phase-in of those capital requirements as the agencies seek public comment on and work to finalize the Simplification Proposal.

The Simplification Proposal would amend the standardized approach for credit risk under the Regulatory Capital Rules by:

- Replacing the definition for high volatility commercial real estate exposures with a simpler definition called "high volatility acquisition, development, or construction" ("HVADC") exposures. The Simplification Proposal would require a banking organization to assign a 130 percent risk weight to HVADC exposures.
- Simplifying the threshold deductions for mortgage servicing assets, temporary difference deferred tax assets that are not realizable through carryback, and investments in the capital of unconsolidated financial institutions. The Simplification Proposal also would revise the risk-weight treatment for investments in the capital of unconsolidated financial institutions.
- Simplifying the limitations on the amount of a third-party minority interest in a consolidated subsidiary that is includable in regulatory capital.

The Simplification Proposal also sets forth clarifying revisions to miscellaneous sections of the Regulatory Capital Rules. If the Simplification Proposal is adopted in its current form as final, it would likely have a neutral-to-low impact on Key's capital requirements, but it would meaningfully alleviate the compliance burden associated with the Regulatory Capital Rules. Comments on the Simplification Proposal are due December 26, 2017.

Capital planning and stress testing

On January 30, 2017, the Federal Reserve released a final rule to revise the capital plan and stress test rules as they apply to large, noncomplex BHCs and U.S. intermediaries of foreign banks. Under the final rule, a large noncomplex BHC is one with total consolidated assets of more than $50 billion but less than $250 billion, and nonbank assets of less than $75 billion ("covered BHCs"). This includes KeyCorp.

The final rule provides relief from the compliance requirements associated with the Federal Reserve's capital plan and stress test rules. Specifically, the final rule relieves covered BHCs from the qualitative assessment portion of the Federal Reserve's CCAR program and modifies the reporting requirements for these organizations by reducing the reporting requirements applicable to covered BHCs under the FR Y-14A and by raising the materiality thresholds for specific portfolio reporting requirements.

The final rule also limits the amount of capital a covered BHC is authorized to distribute in excess of the amount set forth in its capital plan without Federal Reserve approval (the "de minimis exception"), and establishes a one-quarter blackout period during which a BHC is not permitted to submit a notice to use the de minimis exception or seek prior approval to make a capital distribution in an amount that exceeds the de minimis exception level. If exigent circumstances arise during the blackout period that require a capital distribution, a covered BHC may resubmit its capital plan and request expedited review from the Federal Reserve; however, the Federal Reserve is not required to expedite the review process.

The final rule also requires covered BHCs to measure nonbank assets on a monthly basis and report the monthly average to the Federal Reserve on a quarterly basis beginning March 31, 2017.

The final rule became effective 30 days after publication in the Federal Register, and therefore, the relief provided under the final rule from the qualitative assessment portion of the CCAR program is effective for the 2017 CCAR cycle.

On June 9, 2017, the Federal Reserve released a proposal and request for comment on certain information collection activities conducted under the series FR Y-14 schedules and reports that are used in connection with the CCAR program. As they would pertain to Key, the proposed revisions to the FR Y-14A and FR Y-14Q generally consist of modifications to reported items and instructions that would clarify the intended reporting of those items, and seek to further align reported items with the methodology, standards, and treatment in other regulatory reports or with the FR Y-14 schedules. In addition, the Federal Reserve has proposed to eliminate two schedules from the FR Y-14A to reduce the burden, but also to add a new sub-schedule to supplement the existing information collection around business plan change information. Other aspects of the proposal that do not pertain to Key would require the U.S. intermediate holding companies of foreign banks to apply the global market shock adjustment to certain reporting schedules under the FR Y-14A and FR Y-14Q.

Table of Contents

The comment period for the proposed rule ended on August 8, 2017. If the proposal is adopted in its final form, it is expected to have a neutral-to-low impact on Key's reporting and compliance obligations.

Liquidity requirements

In October 2014, the federal banking agencies published a final rule to implement the Basel III liquidity coverage ratio ("Basel III LCR") for U.S. banking organizations (the "Liquidity Coverage Rules") that establishes a minimum LCR for certain internationally active bank and nonbank financial companies (excluding KeyCorp) and a modified version of the LCR ("Modified LCR") for BHCs and other depository institution holding companies with over $50 billion in consolidated assets that are not internationally active (including KeyCorp). KeyBank will not be subject to the LCR or the Modified LCR under the Liquidity Coverage Rules unless the OCC affirmatively determines that application to KeyBank is appropriate in light of KeyBank's asset size, level of complexity, risk profile, scope of operations, affiliation with foreign or domestic covered entities, or risk to the financial system.

Under the Liquidity Coverage Rules, KeyCorp must calculate a Modified LCR on a monthly basis, and was required to satisfy a minimum Modified LCR requirement of 100% by January 1, 2017. At September 30, 2017, Key's Modified LCR was above 100%. In the future, KeyCorp may change the composition of our investment portfolio, increase the size of the overall investment portfolio, and modify product offerings to enhance or optimize our liquidity position.

Net stable funding ratio

The federal banking agencies commenced the U.S. implementation of the Basel III net stable funding ratio ("NSFR") in April and May 2016, with the release of a proposed rule to implement a NSFR requirement for certain internationally active banking organizations (excluding KeyCorp) and a modified version of the minimum NSFR requirement ("Modified NSFR") for BHCs and other depository institution holding companies with over $50 billion in consolidated assets that are not internationally active (including KeyCorp), together with quarterly public disclosure requirements. The proposed rule would require banking organizations to satisfy a minimum NSFR requirement of 1.0 on an ongoing basis. However, banking organizations subject to the Modified NSFR (like KeyCorp) would be required to maintain a lower minimum amount of available stable funding, equal to 70% of the required stable funding under the NSFR. The proposed rule would be effective on January 1, 2018. The comment period for the NPR expired on August 5, 2016. If the proposed NSFR requirement is adopted as a final rule, then similar to actions taken in connection with the implementation of the Liquidity Coverage Rules, KeyCorp may adjust its balance sheet or modify product offerings to enhance its liquidity position.

Resolution and recovery planning

BHCs with at least $50 billion in total consolidated assets, like KeyCorp, are required to periodically submit to the Federal Reserve and FDIC a plan discussing how the company could be rapidly and efficiently resolved if the company failed or experienced material financial distress. Insured depository institutions with at least $50 billion in total consolidated assets, like KeyBank, are also required to submit a resolution plan to the FDIC. These plans are due annually. KeyCorp and KeyBank were not required to submit resolution plans for 2016 because the FDIC and Federal Reserve deferred such requirement until December 2017. By letter dated March 24, 2017, KeyCorp received guidance from the Federal Reserve and the FDIC regarding the information requirements for certain aspects of KeyCorp's December 2017 resolution plan submission. That letter is publicly available on the Federal Reserve's website, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20170324a.htm.

The Federal Reserve and FDIC make available on their websites the public sections of resolution plans for the companies, including KeyCorp and KeyBank, that submitted plans. The public section of the resolution plans of KeyCorp and KeyBank is available at http://www.federalreserve.gov/bankinforeg/resolution-plans.htm and https://www.fdic.gov/regulations/reform/resplans/.

On September 28, 2016, the OCC released final guidelines that establish standards for recovery planning by certain large OCC-regulated institutions, including KeyBank. The guidelines require such institutions to establish a comprehensive framework for evaluating the financial effects of severe stress events, and recovery actions an institution may pursue to remain a viable, going concern during a period of severe financial stress. Under the final guidelines, an institution's recovery plan must include triggers to alert the institution of severe stress events, escalation procedures, recovery options, and a process for periodic review and approval by senior management

Table of Contents

and the board of directors. The recovery plan should be tailored to the complexity, scope of operations, and risk profile of the institution.

Because KeyBank had average total consolidated assets of greater than $100 billion but less than $750 billion as reported on KeyBank's Consolidated Reports of Condition and Income for the four most recent consecutive quarters prior to January 1, 2017, it must be in compliance with the guidelines not later than January 1, 2018.

Deposit insurance and assessments

As required under the Dodd-Frank Act, in March 2015, the FDIC approved a final rule to impose a surcharge on the quarterly deposit insurance assessments of insured depository institutions having total consolidated assets of at least $10 billion (like KeyBank). The surcharge is 4.5 cents per $100 of the institution's assessment base (after making certain adjustments). The final rule became effective on July 1, 2016. As of July 1, 2016, KeyBank must pay a surcharge to assist in bringing the reserve ratio to the statutory minimum of 1.35%. Surcharges will continue through the quarter that the DIF reserve ratio reaches or exceeds 1.35%, but not later than December 31, 2018. If the reserve ratio does not reach 1.35% by December 31, 2018 (provided it is at least 1.15%), the FDIC will impose a shortfall assessment on March 31, 2019, on insured depository institutions with total consolidated assets of $10 billion or more (like KeyBank). At June 30, 2017, the DIF reserve ratio was 1.24%.

In December 2016, the FDIC issued a final rule that imposes recordkeeping requirements on insured depository institutions with two million or more deposit accounts (including KeyBank) in order to facilitate rapid payment of insured deposits to customers if the institutions were to fail. The rule requires those insured depository institutions to: (i) maintain complete and accurate data on each depositor's ownership interest by right and capacity for all of the institution's deposit accounts; and (ii) develop the capability to calculate the insured and uninsured amounts for each deposit owner within 24 hours of failure. The FDIC will conduct periodic testing of compliance with these requirements, and institutions subject to the rule must submit to the FDIC a certification of compliance, signed by the KeyBank chief executive officer, and deposit insurance coverage summary report on or before the mandatory compliance date and annually thereafter. The final rule became effective on April 1, 2017, with a mandatory compliance date of April 1, 2020.

Single counterparty credit limits

In March 2016, the Federal Reserve issued an NPR proposing to establish single counterparty credit limits for BHCs with total consolidated assets of $50 billion or more. This proposal would implement a provision in the Dodd-Frank Act and replaces proposals on this subject issued by the Federal Reserve in 2011 and 2012. Under the proposal, a covered BHC (including KeyCorp) would not be allowed to have an aggregate net credit exposure to any unaffiliated counterparty that exceeds 25% of the consolidated capital stock and surplus of the covered BHC. Globally, systemically important banks and certain other large BHCs (excluding KeyCorp) would be subject to stricter limits under the proposal. A covered BHC such as KeyCorp would be required to comply with the proposed limits and quarterly reporting to show such compliance starting two years after the effective date of a final rule. The comment period for the NPR expired on June 3, 2016.

Supervision and governance

On August 3, 2017, the Federal Reserve released a proposal to establish guidance regarding supervisory expectations for the boards of directors of banking organizations with total consolidated assets of $50 billion or more, including KeyCorp. The proposal identifies the attributes of effective boards of directors that would be used for examiner evaluation of an organization's governance and controls. The proposal also clarifies that for all organizations supervised by the Federal Reserve, most supervisory findings should be communicated to the organization's senior management for corrective action and not its board of directors. In addition, the proposal identifies existing supervisory expectations for boards of directors set forth in Federal Reserve SR Letters that could be eliminated or revised. Comments on the proposal are due November 30, 2017.

In a separate release, the Federal Reserve published a notice of proposed rulemaking to align its supervisory rating system for large financial institutions (including KeyCorp) with the post-crisis supervisory programs for these firms. The proposed rating system would only apply to large financial institutions, including KeyCorp, and would evaluate and assign ratings to large financial institutions based on three components: capital planning and positions, liquidity risk management and positions, and governance and controls. It is difficult to estimate the potential impact of the proposal on Key because the extent of the impact depends on the finalization of the proposal regarding supervisory

Table of Contents

expectations for boards of directors, and a forthcoming proposal regarding supervisory expectations relating to a firm's management of core business lines and independent risk management and controls. Moreover, implementation of the proposed rating system could involve considerable examiner discretion. Comments are due on the proposed rule by November 30, 2017.

ERISA fiduciary standard

In April 2016, the Department of Labor published final rules and amendments to certain prohibited transaction exemptions regarding which service providers would be regarded as fiduciaries under ERISA for making investment advice recommendations to: (i) certain retirement plan fiduciaries, participants, or beneficiaries; and (ii) owners or beneficiaries of individual retirement accounts and health savings accounts, among other retirement plans. The purpose of the rules is to place fiduciary obligations, rather than the lesser legal obligations that currently apply, on these service providers. Accordingly, the rules subject any financial institution making recommendations for either the purchase or sale of investments in or rollover of the respective retirement plan to certain fiduciary obligations under ERISA such as an impartial conduct standard and not selling certain investment products whose compensation may raise a conflict of interest for the advisor without entering into a contract providing certain disclosures and legal remedies to the customer. Under the Department of Labor's original rules, the impartial standard requirement for financial institutions and their advisors was to become effective April 10, 2017. However, in response to a Presidential Order, the Department of Labor extended the effective date to June 9, 2017. The contract provisions must be in place by January 1, 2018, although on August 31, 2017, the Department of Labor requested comments on a proposal to delay this date until July 1, 2019. The Department of Labor also requested comments on and will continue to review whether to modify, further delay, or rescind these rules in whole or in part.

Highlights of Our Performance

Financial performance

For the third quarter of 2017, we announced net income from continuing operations attributable to Key common shareholders of $349 million, or $.32 per common share. Our third quarter of 2017 results compare to net income from continuing operations attributable to Key common shareholders of $165 million, or .16 per common share, for the third quarter of 2016. During the third quarter of 2017, our results included $36 million of merger-related charges and a $5 million merchant services gain adjustment, resulting in a pre-tax net impact of $41 million, or $.03 per common share.

Third quarter 2017 net interest income included $48 million of purchase accounting accretion related to the acquisition of First Niagara.

Our TE net interest income was $962 million for the third quarter of 2017, and the net interest margin was 3.15%, compared to TE net interest income of $788 million and a net interest margin of 2.85% for the third quarter of 2016, reflecting the benefit from the First Niagara acquisition, including purchase accounting accretion, as well as higher earning asset yields and balances. Excluding purchase accounting accretion, taxable-equivalent net interest income increased $145 million from the third quarter of 2016. For the full year of 2017, we expect net interest income to be in the range of $3.8 billion to $3.9 billion. Our outlook does not include any additional rate increases in 2017.

Our noninterest income was $592 million for the third quarter of 2017, compared to $549 million for the year-ago quarter. Growth was largely driven by a full-quarter impact of the First Niagara acquisition, as well as ongoing momentum in our core businesses. Broad-based growth across many fee income categories more than offset a decline in investment banking and debt placement fees, related to strong market conditions in the year-ago period. For the full year of 2017, we expect noninterest income to be in the range of $2.35 billion to $2.45 billion.

Our noninterest expense was $992 million for the third quarter of 2017, which included $36 million of merger-related charges. Merger-related charges for the quarter were made up of $25 million of personnel expense and $11 million of non-personnel expense, mostly reflected in marketing and computer processing expense. During the third quarter of 2016, we incurred $189 million of merger-related charges.

Excluding merger-related charges, noninterest expense was $63 million higher than the third quarter of last year. The increase from the prior year, reflected in both personnel and non-personnel expense, was primarily driven by a full-quarter impact of the First Niagara acquisition, as well as ongoing business investments and recent acquisitions, partially offset by merger cost savings. Professional fees were also elevated due to several short-term initiatives.

Table of Contents

While our recent acquisitions of HelloWallet and Key Merchant Services, LLC will be accretive over time, together they added $8 million of expense for the third quarter of 2017. For the full year of 2017, we expect noninterest expense excluding merger-related charges to be in the range of $3.7 billion to $3.8 billion. Included within this range is approximately $20 million in added expense from Cain Brothers, which closed early in the fourth quarter of 2017, as well as expenses related to HelloWallet and Key Merchant Services, LLC.

Average loans were $86.8 billion for the third quarter of 2017, an increase of $9.1 billion compared to the third quarter of 2016, primarily reflecting a full-quarter impact of the First Niagara acquisition, as well as growth in commercial and industrial loans, which was broad-based and spread across Key's commercial lines of business. We anticipate average loans to be in the range of $87 billion to $87.5 billion for the fourth quarter of 2017.

Average deposits totaled $103.1 billion for the third quarter of 2017, an increase of $8.2 billion compared to the year-ago quarter, primarily reflecting a full-quarter impact of the First Niagara acquisition, and core retail and commercial deposit growth. Our consolidated loan-to-deposit ratio was 86.2% at September 30, 2017, compared to 84.7% at September 30, 2016. We anticipate average deposits to be in the range of $102.5 billion to $103 billion for the fiscal year 2017.

Our provision for credit losses was $51 million for the third quarter of 2017, compared to $59 million for the third quarter of 2016. The third quarter 2017 provision reflects a large recovery in the commercial and industrial portfolio. Our allowance for loan and lease losses was $880 million, or 1.02% of total period-end loans, at September 30, 2017, compared to 1.01% at September 30, 2016. For the remainder of 2017, we expect the provision for credit losses to slightly exceed net loan charge-offs to provide for loan growth.

Net loan charge-offs for the third quarter of 2017 totaled $32 million, or .15% of average total loans, compared to $44 million, or .23%, for the third quarter of 2016. For the remainder of 2017, we expect net loan charge-offs to average loans to remain below our targeted range of 40 to 60 basis points.

At September 30, 2017, our nonperforming loans totaled $517 million, which represented .60% of period-end portfolio loans, compared to $723 million, or 0.85% of period-end portfolio loans, at September 30, 2016. Nonperforming assets at September 30, 2017, totaled $556 million and represented .64% of period-end portfolio loans and OREO and other nonperforming assets, compared to $760 million, or .89% of period-end portfolio loans and OREO and other nonperforming assets, at September 30, 2016.

Our capital ratios remain strong. Our tangible common equity and Tier 1 risk-based capital ratios at September 30, 2017, are 8.49% and 11.11%, respectively, compared to 8.27% and 10.53%, respectively, at September 30, 2016. In addition, our Common Equity Tier 1 ratio is 10.26% at September 30, 2017, compared to 9.56% at September 30, 2016. Capital levels in the third quarter of 2017 benefited from a change in our methodology related to risk weightings for multipurpose facilities, specifically commitments that can also be used for letters of credit.

We continue to return capital to our shareholders by repurchasing Common Shares and through our quarterly common share dividend. In the third quarter of 2017, we completed $277 million of Common Share repurchases, including $271 million of common share repurchases in the open market and $6 million of Common Share repurchases related to employee equity compensation programs, and paid a cash dividend of $.095 per Common Share, under our 2017 capital plan authorization.

Figure 5 shows our continuing and discontinued operating results for the current, past, and year-ago quarters. Our financial performance for each of the past five quarters is summarized in Figure 1.

16

Table of Contents

Figure 5. Results of Operations

	Three months ended			Nine months ended	
in millions, except per share amounts	9/30/2017	6/30/2017	9/30/2016	9/30/2017	9/30/2016
Summary of operations					
Income (loss) from continuing operations attributable to Key	$363	$ 407	$ 171	$1,094	$ 557
Income (loss) from discontinued operations, net of taxes [a]	1	5	1	6	5
Net income (loss) attributable to Key	$364	$ 412	$ 172	$1,100	$ 562
Income (loss) from continuing operations attributable to Key	$363	$ 407	$ 171	$1,094	$ 557
Less: Dividends on Preferred Stock	14	14	6	56	17
Income (loss) from continuing operations attributable to Key common shareholders	349	393	165	1,038	540
Income (loss) from discontinued operations, net of taxes [a]	1	5	1	6	5
Net income (loss) attributable to Key common shareholders	$350	$ 398	$ 166	$1,044	$ 545
Per common share — assuming dilution					
Income (loss) from continuing operations attributable to Key common shareholders	$.32	$ .36	$ .16	$.95	$ .60
Income (loss) from discontinued operations, net of taxes [a]	—	—	—	.01	.01
Net income (loss) attributable to Key common shareholders [b]	$.32	$ .36	$ .17	$.96	$ .61

(a) In September 2009, we decided to discontinue the education lending business conducted through Key Education Resources, the education payment and financing unit of KeyBank. As a result of this decision, we have accounted for these businesses as a discontinued operation. For further discussion regarding the income (loss) from discontinued operations, see Note 12 ("Acquisition, Divestiture, and Discontinued Operations").

(b) EPS may not foot due to rounding.

Figure 6 presents certain non-GAAP financial measures related to "tangible common equity," "return on tangible common equity," "cash efficiency ratio," certain financial measures excluding notable items, and "Common Equity Tier 1 under the Regulatory Capital Rules (estimates)."

Notable items include certain revenue or expense items that may occur in a reporting period which management does not consider indicative of ongoing financial performance. Management believes it is useful to consider certain financial metrics with and without merger-related charges and/or other notable items in order to enable a better understanding of Company results, increase comparability of period-to-period results, and to evaluate and forecast those results.

The tangible common equity ratio and the return on tangible common equity ratio have been a focus for some investors, and management believes that these ratios may assist investors in analyzing Key's capital position without regard to the effects of intangible assets and preferred stock. Since analysts and banking regulators may assess our capital adequacy using tangible common equity, we believe it is useful to enable investors to assess our capital adequacy on these same bases. Figure 6 reconciles the GAAP performance measures to the corresponding non-GAAP measures.

As disclosed in Note 2 ("Business Combination") and Note 12 ("Acquisition, Divestiture, and Discontinued Operations"), KeyCorp completed its purchase of First Niagara on August 1, 2016. The definitive agreement and plan of merger to acquire First Niagara was originally announced on October 30, 2015. As a result of this transaction, we've recognized merger-related charges. For the second and third quarters of 2017, merger-related charges are included in the total for "notable items." The table below shows the computation of return on average tangible common equity excluding notable items, pre-provision net revenue excluding notable items, cash efficiency ratio excluding notable items, and return on average assets from continuing operations excluding notable items. Management believes that eliminating the effects of the merger-related charges and other notable items makes it easier to analyze the results by presenting them on a more comparable basis.

The cash efficiency ratio is a ratio of two non-GAAP performance measures. Accordingly, there is no directly comparable GAAP performance measure. The cash efficiency ratio excludes the impact of our intangible asset amortization from the calculation. We also disclose the cash efficiency ratio excluding notable items. We believe these ratios provide greater consistency and comparability between our results and those of our peer banks. Additionally, these ratios are used by analysts and investors as they develop earnings forecasts and peer bank analysis.

Non-GAAP financial measures have inherent limitations, are not required to be uniformly applied, and are not audited. Although these non-GAAP financial measures are frequently used by investors to evaluate a company, they have limitations as analytical tools, and should not be considered in isolation, nor as a substitute for analyses of results as reported under GAAP.

Table of Contents

Figure 6. GAAP to Non-GAAP Reconciliations

	Three months ended					Nine months ended	
dollars in millions	9/30/2017	6/30/2017	3/31/2017	12/31/2016	9/30/2016	9/30/2017	9/30/2016
Tangible common equity to tangible assets at period-end							
Key shareholders' equity (GAAP)	$15,249	$15,253	$14,976	$15,240	$14,996		
Less: Intangible assets [a]	2,870	2,866	2,751	2,788	2,855		
Preferred Stock [b]	1,009	1,009	1,009	1,640	1,150		
Tangible common equity (non-GAAP)	$11,370	$11,378	$11,216	$10,812	$10,991		
Total assets (GAAP)	$136,733	$135,824	$134,476	$136,453	$135,805		
Less: Intangible assets [a]	2,870	2,866	2,751	2,788	2,855		
Tangible assets (non-GAAP)	$133,863	$132,958	$131,725	$133,665	$132,950		
Tangible common equity to tangible assets ratio (non-GAAP)	8.49 %	8.56 %	8.51 %	8.09 %	8.27 %		
Notable items							
Merger-related charges	$(36)	$(44)	$(81)	$(198)	(207)	$(161)	$(276)
Merchant services gain	(5)	64	—	—	—	59	—
Purchase accounting finalization, net	—	43	—	—	—	43	—
Charitable contribution	—	(20)	—	—	—	(20)	—
Total notable items	$(41)	$43	$(81)	$(198)	(207)	$(79)	$(276)
Income taxes	(13)	16	(30)	(74)	(75)	(27)	(101)
Total notable items after tax	$(28)	$27	$(51)	$(124)	(132)	$(52)	$(175)
Average tangible common equity							
Average Key shareholders' equity (GAAP)	$15,241	$15,200	$15,184	$14,901	$13,552	$15,208	$11,890
Less: Intangible assets (average) [c]	2,878	2,756	2,772	2,874	2,255	2,802	1,473
Preferred Stock (average)	1,025	1,025	1,480	1,274	648	1,175	410
Average tangible common equity (non-GAAP)	$11,338	$11,419	$10,932	$10,753	$10,649	$11,231	$10,007
Return on average tangible common equity from continuing operations							
Net income (loss) from continuing operations attributable to Key common shareholders (GAAP)	$349	$393	$296	$213	$165	$1,038	$540
Plus: Notable items, after tax	28	(27)	51	124	132	52	175
Net income (loss) from continuing operations attributable to Key common shareholders after	$377	$366	$347	$337	$297	$1,090	$715

	notable items (non-GAAP)							
Average tangible common equity (non-GAAP)		11,338	11,419	10,932	10,753	10,649	11,231	10,007
Return on average tangible common equity from continuing operations (non-GAAP)		12.21 %	13.80 %	10.98 %	7.88 %	6.16 %	12.36 %	7.21 %
Return on average tangible common equity from continuing operations excluding notable items (non-GAAP)		13.19	12.86	12.87	12.47	11.10	12.98	9.54
Return on average tangible common equity consolidated								
Net income (loss) attributable to Key common shareholders (GAAP)		$350	$398	$296	$209	$166	$1,044	$545
Average tangible common equity (non-GAAP)		11,338	11,419	10,932	10,753	10,649	11,231	10,007
Return on average tangible common equity consolidated (non-GAAP)		12.25 %	13.98 %	10.98 %	7.73 %	6.20 %	12.43 %	7.27 %
Pre-provision net revenue								
Net interest income (GAAP)		$948	$973	$918	$938	$780	$2,839	$1,981
Plus:	Taxable-equivalent adjustment	14	14	11	10	8	39	24
	Noninterest income (GAAP)	592	653	577	618	549	1,822	1,453
Less:	Noninterest expense (GAAP)	992	995	1,013	1,220	1,082	3,000	2,536
	Pre-provision net revenue from continuing operations (non-GAAP)	$562	$645	$493	$346	$255	$1,700	$922
Plus:	Notable items	36	(43)	81	198	207	79	276
	Pre-provision net revenue from continuing operations excluding notable items (non-GAAP)	603	602	574	544	462	1,779	1,198
Cash efficiency ratio								
Noninterest expense (GAAP)		$992	$995	$1,013	$1,220	$1,082	$3,000	$2,536
Less:	Intangible asset amortization	25	22	22	27	13	69	28
Adjusted noninterest expense (non-GAAP)		$967	$973	$991	$1,193	$1,069	$2,931	$2,508
Less:	Notable items [d]	36	60	81	207	189	177	258
Adjusted noninterest expense excluding notable items (non-GAAP)		$931	$913	$910	$986	$880	$2,754	$2,250
Net interest income (GAAP)		$948	$973	$918	$938	$780	$2,839	$1,981
Plus:	Taxable-equivalent adjustment	14	14	11	10	8	39	24
	Noninterest income (GAAP)	592	653	577	618	549	1,822	1,453

Total taxable-equivalent revenue (non-GAAP)	$1,554	$1,640	$1,506	$1,566	$1,337	$4,700	$3,458
Plus: Notable items (e)	5	(103)	—	(9)	18	(98)	18
Adjusted noninterest income excluding notable items (non-GAAP)	$1,559	$1,537	$1,506	$1,557	$1,355	$4,602	$3,476
Cash efficiency ratio (non-GAAP)	62.2 %	59.3 %	65.8 %	76.2 %	80.0 %	62.4 %	72.5 %
Cash efficiency ratio excluding notable items (non-GAAP)	59.7	59.4	60.4	63.3	64.9	59.8	64.7
Return on average total assets from continuing operations excluding notable items							
Income from continuing operations attributable to Key (GAAP)	$363	$407	$324	$233	$171	$1,094	$557
Plus: Notable items, after tax	28	(27)	51	124	132	52	175
Income from continuing operations attributable to Key excluding notable items, after tax (non-GAAP)	$391	$380	$375	$357	$303	$1,146	$732
Average total assets from continuing operations (GAAP)	$134,356	$132,491	$132,741	$134,428	$123,469	$133,202	$105,187
Return on average total assets from continuing operations excluding notable items (non-GAAP)	1.15 %	1.15 %	1.15 %	1.06 %	.98 %	1.15 %	.93 %

18

Table of Contents

Figure 6. GAAP to Non-GAAP Reconciliations, continued

dollars in millions	Three months ended September 30, 2017
Common Equity Tier 1 under the Regulatory Capital Rules (estimates)	
Common Equity Tier 1 under current Regulatory Capital Rules	$ 12,129
Adjustments from current Regulatory Capital Rules to the fully phased-in Regulatory Capital Rules:	
Deferred tax assets and other intangible assets [(f)]	(57)
Common Equity Tier 1 anticipated under the fully phased-in Regulatory Capital Rules [(g)]	$ 12,072
Net risk-weighted assets under current Regulatory Capital Rules	$ 118,233
Adjustments from current Regulatory Capital Rules to the fully phased-in Regulatory Capital Rules:	
Mortgage servicing assets [(h)]	623
Volcker Funds	—
All other assets	49
Total risk-weighted assets anticipated under the fully phased-in Regulatory Capital Rules [(g)]	$ 118,905
Common Equity Tier 1 ratio under the fully phased-in Regulatory Capital Rules [(g)]	10.15 %

(a) For the three months ended September 30, 2017, June 30, 2017, March 31, 2017, December 31, 2016, and September 30, 2016, intangible assets exclude $30 million, $33 million, $38 million, $42 million, and $51 million, respectively, of period-end purchased credit card relationships.

(b) Net of capital surplus.

(c) For the three months ended September 30, 2017, June 30, 2017, March 31, 2017, December 31, 2016, and September 30, 2016, average intangible assets exclude $32 million, $36 million, $40 million, $46 million, and $47 million, respectively, of average purchased credit card relationships. For the nine months ended September 30, 2017, and September 30, 2016, average intangible assets exclude $36 million and $42 million, respectively, of average purchased credit card receivables.

(d) Notable items for the three months ended September 30, 2017, include $36 million of merger-related expense.

(e) Notable items for the three months ended September 30, 2017, include $5 million adjustment related to the merchant services acquisition gain.

(f) Includes the deferred tax assets subject to future taxable income for realization, primarily tax credit carryforwards, as well as intangible assets (other than goodwill and mortgage servicing assets) subject to the transition provisions of the final rule.

(g) The anticipated amount of regulatory capital and risk-weighted assets is based upon the federal banking agencies' Regulatory Capital Rules (as fully phased-in on January 1, 2019); we are subject to the Regulatory Capital Rules under the "standardized approach."

(h) Item is included in the 10%/15% exceptions bucket calculation and is risk-weighted at 250%.

Results of Operations

Net interest income

One of our principal sources of revenue is net interest income. Net interest income is the difference between interest income received on earning assets (such as loans and securities) and loan-related fee income, and interest expense paid on deposits and borrowings. There are several factors that affect net interest income, including:

- the volume, pricing, mix, and maturity of earning assets and interest-bearing liabilities;

- the volume and value of net free funds, such as noninterest-bearing deposits and equity capital;
- the use of derivative instruments to manage interest rate risk;
- interest rate fluctuations and competitive conditions within the marketplace;
- asset quality; and
- fair value accounting of acquired earning assets and interest-bearing liabilities.

To make it easier to compare both the results across several periods and the yields on various types of earning assets (some taxable, some not), we present net interest income in this discussion on a "TE basis" (i.e., as if all income were taxable and at the same rate). For example, $100 of tax-exempt income would be presented as $154, an amount that, if taxed at the statutory federal income tax rate of 35%, would yield $100.

Figure 7 shows the various components of our balance sheet that affect interest income and expense, and their respective yields or rates over the past five quarters. This figure also presents a reconciliation of TE net interest income to net interest income reported in accordance with GAAP for each of those quarters. The net interest margin, which is an indicator of the profitability of the earning assets portfolio less cost of funding, is calculated by dividing annualized TE net interest income by average earning assets.

Third quarter 2017 TE net interest income included $48 million of purchase accounting accretion related to the acquisition of First Niagara, compared to $19 million in the third quarter of 2016, and $100 million in the second quarter of 2017.

TE net interest income was $962 million for the third quarter of 2017, and the net interest margin was 3.15%, compared to TE net interest income of $788 million and a net interest margin of 2.85% for the third quarter of 2016, reflecting the full quarter benefit from the First Niagara acquisition, including purchase accounting accretion, as well as higher earning asset yields and balances.

For the nine months ended September 30, 2017, TE net interest income was $2.9 billion and the net interest margin was 3.19%, compared to TE net interest income of $2.0 billion and a net interest margin of 2.84% for the prior year, reflecting the full year-to-date benefit from the First Niagara acquisition, growth in our core earning asset balances, higher interest rates, and managed deposit costs.

Average loans were $86.8 billion for the third quarter of 2017, an increase of $9.1 billion compared to the third quarter of 2016, primarily reflecting a full-quarter impact of the First Niagara acquisition, as well as growth in commercial and industrial loans, which was broad-based and spread across Key's commercial lines of business. At September 30, 2017, the remaining fair value discount on the First Niagara acquired loan portfolio was $302 million, compared to $345 million at June 30, 2017.

Average deposits totaled $103.1 billion for the third quarter of 2017, an increase of $8.2 billion compared to the year-ago quarter, primarily reflecting a full-quarter impact of the First Niagara acquisition, and core retail and commercial deposit growth.

Table of Contents

Figure 7. Consolidated Average Balance Sheets, Net Interest Income, and Yields/Rates from Continuing Operations

	Third Quarter 2017			Second Quarter 2017		
dollars in millions	Average Balance	Interest [a]	Yield/ Rate [a]	Average Balance	Interest [a]	Yield/ Rate [a]
ASSETS						
Loans [b], [c]						
Commercial and industrial [d]	$41,416	$ 414	3.97 %	$40,666	$ 409	4.04 %
Real estate — commercial mortgage	14,850	169	4.51	15,096	187	4.97
Real estate — construction	2,054	23	4.51	2,204	31	5.51
Commercial lease financing	4,694	46	3.89	4,690	50	4.33
Total commercial loans	63,014	652	4.11	62,656	677	4.34
Real estate — residential mortgage	5,493	54	3.92	5,509	52	3.77
Home equity loans	12,314	136	4.41	12,473	135	4.31
Consumer direct loans	1,774	33	7.26	1,743	31	7.07
Credit cards	1,049	30	11.34	1,044	29	11.04
Consumer indirect loans	3,170	37	4.64	3,077	38	5.02
Total consumer loans	23,800	290	4.85	23,846	285	4.77
Total loans	86,814	942	4.31	86,502	962	4.46
Loans held for sale	1,607	17	4.13	1,082	9	3.58
Securities available for sale [b], [e]	18,574	91	1.96	17,997	90	1.97
Held-to-maturity securities [b]	10,469	55	2.12	10,469	55	2.09
Trading account assets	889	7	2.74	1,042	7	3.00
Short-term investments	2,166	6	1.21	1,970	5	.96
Other investments [e]	728	5	2.46	687	3	1.87
Total earning assets	121,247	1,123	3.68	119,749	1,131	3.78
Allowance for loan and lease losses	(868)			(864)		
Accrued income and other assets	13,977			13,606		
Discontinued assets	1,417			1,477		
Total assets	$135,773			$133,968		
LIABILITIES						
NOW and money market deposit accounts	$53,826	37	.27	$54,416	34	.25
Savings deposits	6,697	5	.25	6,854	4	.21
Certificates of deposit ($100,000 or more)	6,402	21	1.31	6,111	19	1.23
Other time deposits	4,664	9	.81	4,650	9	.77
Total interest-bearing deposits	71,589	72	.40	72,031	66	.36
Federal funds purchased and securities sold under repurchase agreements	456	—	.23	466	—	.23
Bank notes and other short-term borrowings	865	3	1.49	1,216	4	1.43
Long-term debt [f], [g]	12,631	86	2.75	11,046	74	2.68
Total interest-bearing liabilities	85,541	161	.75	84,759	144	.68
Noninterest-bearing deposits	31,516			30,748		
Accrued expense and other liabilities	2,057			1,782		
Discontinued liabilities [g]	1,417			1,477		
Total liabilities	120,531			118,766		
EQUITY						
Key shareholders' equity	15,241			15,200		
Noncontrolling interests	1			2		

Total equity	15,242			15,202		
Total liabilities and equity	$135,773			$133,968		
Interest rate spread (TE)			2.93 %			3.10 %
Net interest income (TE) and net interest margin (TE)		962	3.15 %		987	3.30 %
TE adjustment [b]		14			14	
Net interest income, GAAP basis		$ 948			$ 973	

(a) Results are from continuing operations. Interest excludes the interest associated with the liabilities referred to in (g) below, calculated using a matched funds transfer pricing methodology.

(b) Interest income on tax-exempt securities and loans has been adjusted to a TE basis using the statutory federal income tax rate of 35%.

(c) For purposes of these computations, nonaccrual loans are included in average loan balances.

(d) Commercial and industrial average balances include $117 million, $117 million, $114 million, $119 million, and $107 million of assets from commercial credit cards for the three months ended September 30, 2017, June 30, 2017, March 31, 2017, December 31, 2016, and September 30, 2016, respectively.

Table of Contents

Figure 7. Consolidated Average Balance Sheets, Net Interest Income, and Yields/Rates from Continuing Operations

First Quarter 2017			Fourth Quarter 2016			Third Quarter 2016		
Average Balance	Interest [a]	Yield/ Rate [a]	Average Balance	Interest [a]	Yield/ Rate [a]	Average Balance	Interest [a]	Yield/ Rate [a]
$40,002	$ 373	3.77 %	$39,495	$ 365	3.68 %	$37,318	$ 317	3.38 %
15,187	164	4.39	14,771	168	4.50	12,879	126	3.91
2,353	26	4.54	2,222	37	6.72	1,723	21	4.67
4,635	44	3.76	4,624	50	4.34	4,508	38	3.33
62,177	607	3.95	61,112	620	4.04	56,428	502	3.54
5,520	54	3.94	5,554	57	4.17	4,453	45	3.96
12,611	131	4.22	12,812	129	3.99	11,968	122	4.07
1,762	30	6.97	1,785	31	6.84	1,666	30	7.20
1,067	29	11.06	1,088	29	10.78	996	27	10.80
2,996	37	4.91	3,009	42	5.50	2,186	28	5.23
23,956	281	4.75	24,248	288	4.73	21,269	252	4.73
86,133	888	4.17	85,360	908	4.24	77,697	754	3.86
1,188	13	4.28	1,323	11	3.39	1,152	10	3.48
19,181	95	1.95	20,145	92	1.82	17,972	88	1.99
9,988	51	2.04	9,121	44	1.95	6,250	30	1.86
968	7	2.75	892	6	2.54	860	4	2.12
1,610	3	.79	3,717	5	.49	5,911	7	.48
709	4	2.26	741	6	3.23	717	5	2.74
119,777	1,061	3.57	121,299	1,072	3.52	110,559	898	3.24
(855)			(855)			(847)		
13,819			13,984			13,757		
1,540			1,610			1,676		
$134,281			$136,038			$125,145		
$54,295	32	.24	$55,444	31	.22	$51,318	25	.20
6,351	1	.10	6,546	2	.10	4,521	1	.07
5,627	16	1.16	5,428	15	1.11	4,204	12	1.15
4,706	9	.76	4,849	9	.77	5,031	11	.85
70,979	58	.33	72,267	57	.32	65,074	49	.30
795	1	.32	592	1	.11	578	—	.16
1,802	5	1.06	934	3	1.11	1,186	2	.91
10,833	68	2.54	10,914	63	2.38	10,415	59	2.31
84,409	132	.63	84,707	124	.58	77,253	110	.57
31,099			32,424			29,844		
2,048			2,394			2,818		
1,540			1,610			1,676		
119,096			121,135			111,591		
15,184			14,901			13,552		
1			2			2		
15,185			14,903			13,554		
$134,281			$136,038			$125,145		

	2.94 %		2.94 %		2.67 %
929	3.13 %	948	3.12 %	788	2.85 %
11		10		8	
$ 918		$ 938		$ 780	

(e) Yield is calculated on the basis of amortized cost.

(f) Rate calculation excludes basis adjustments related to fair value hedges.

(g) A portion of long-term debt and the related interest expense is allocated to discontinued liabilities as a result of applying our matched funds transfer pricing methodology to discontinued operations.

22

Table of Contents

Figure 8 shows how the changes in yields or rates and average balances from the prior year period affected net interest income. The section entitled "Financial Condition" contains additional discussion about changes in earning assets and funding sources.

Figure 8. Components of Net Interest Income Changes from Continuing Operations

in millions	From three months ended September 30, 2016 to three months ended September 30, 2017			From nine months ended September 30, 2016 to nine months ended September 30, 2017		
	Average Volume	Yield/Rate	Net Change [(a)]	Average Volume	Yield/Rate	Net Change [(a)]
INTEREST INCOME						
Loans	$94	$94	$188	$627	$266	$893
Loans held for sale	5	2	7	13	3	16
Securities available for sale	3	—	3	46	(7)	39
Held-to-maturity securities	22	3	25	78	5	83
Trading account assets	—	3	3	2	2	4
Short-term investments	(6)	5	(1)	(15)	12	(3)
Other investments	—	—	—	1	1	2
Total interest income (TE)	118	107	225	752	282	1,034
INTEREST EXPENSE						
NOW and money market deposit accounts	1	11	12	17	30	47
Savings deposits	1	3	4	2	7	9
Certificates of deposit ($100,000 or more)	7	2	9	25	(2)	23
Other time deposits	(1)	(1)	(2)	5	(2)	3
Total interest-bearing deposits	8	15	23	49	33	82
Federal funds purchased and securities sold under repurchase agreements	—	—	—	—	1	1
Bank notes and other short-term borrowings	(1)	2	1	4	1	5
Long-term debt	14	13	27	38	35	73
Total interest expense	21	30	51	91	70	161
Net interest income (TE)	$97	$77	$174	$661	$212	$873

(a) The change in interest not due solely to volume or rate has been allocated in proportion to the absolute dollar amounts of the change in each.

Noninterest income

As shown in Figure 9, noninterest income was $592 million for the third quarter of 2017, compared to $549 million for the year-ago quarter. For the nine months ended September 30, 2017, noninterest income was $1.8 billion compared to $1.5 billion for the same period one year ago. Noninterest income represented 38% and 39% of total revenue for the three and nine months ended September 30, 2017, respectively, compared to 41% and 42% for the three and nine months ended September 30, 2016, respectively.

The following discussion explains the composition of certain elements of our noninterest income and the factors that caused those elements to change.

Figure 9. Noninterest Income

dollars in millions	Three months ended September 30, 2017	2016	Change Amount	Percent	Nine months ended September 30, 2017	2016	Change Amount	Percent
Trust and investment services income	$135	$122	$13	10.7 %	$404	$341	$63	18.5 %
Investment banking and debt placement fees	141	156	(15)	(9.6)	403	325	78	24.0
Service charges on deposit accounts	91	85	6	7.1	268	218	50	22.9
Operating lease income and other leasing gains	16	6	10	166.7	69	41	28	68.3
Corporate services income	54	51	3	5.9	163	154	9	5.8
Cards and payments income	75	66	9	13.6	210	164	46	28.0
Corporate-owned life insurance income	31	29	2	6.9	94	85	9	10.6
Consumer mortgage income	7	6	1	16.7	19	11	8	72.7
Mortgage servicing fees	21	15	6	40.0	54	37	17	45.9
Net gains (losses) from principal investing	3	5	(2)	(40.0)	4	16	(12)	(75.0)
Other income	18	8	10	125.0	134	61	73	119.7
Total noninterest income	$592	$549	$43	7.8 %	$1,822	$1,453	$369	25.4 %

Table of Contents

Trust and investment services income

Trust and investment services income consists of brokerage commissions, trust and asset management commissions, and insurance income. The assets under management that primarily generate these revenues are shown in Figure 10. For the three months ended September 30, 2017, trust and investment services income increased $13 million, or 10.7%, compared to the same period one year ago, primarily due to an increase in insurance income as a result of the First Niagara acquisition and fees earned from investment management services as a result of stronger market performance.

For the nine months ended September 30, 2017, trust and investment services income was up $63 million, or 18.5%, from the nine months ended September 30, 2016, primarily due to an increase in insurance income and brokerage commissions as a result of the acquisition of First Niagara and higher fees earned from investment management services as a result of stronger market performance.

A significant portion of our trust and investment services income depends on the value and mix of assets under management. At September 30, 2017, our bank, trust, and registered investment advisory subsidiaries had assets under management of $38.7 billion, compared to $36.8 billion at September 30, 2016. The increase in assets under management, as shown in Figure 10, was primarily attributable to market appreciation over the past twelve months.
Figure 10. Assets Under Management

in millions	September 30, 2017	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016
Assets under management by investment type:					
Equity	$ 23,342	$ 22,824	$ 22,522	$ 21,722	$ 21,568
Securities lending	876	807	1,095	1,148	991
Fixed income	11,009	10,819	10,497	10,386	11,016
Money market	3,433	3,163	3,303	3,336	3,177
Total assets under management	$ 38,660	$ 37,613	$ 37,417	$ 36,592	$ 36,752

Investment banking and debt placement fees

Investment banking and debt placement fees consists of syndication fees, debt and equity financing fees, financial adviser fees, gains on sales of commercial mortgages, and agency origination fees. Investment banking and debt placement fees decreased $15 million, or 9.6%, for the third quarter of 2017, related to strong market conditions in the year-ago period.

For the nine months ended September 30, 2017, investment banking and debt placement fees increased $78 million, or 24.0%, from the same period one year ago driven by stronger market conditions.

Service charges on deposit accounts

Service charges on deposit accounts increased $6 million, or 7.1%, for the three months ended September 30, 2017, compared to the same period one year ago. The increase from the three months ended September 30, 2016, was primarily due to the full-quarter impact of the First Niagara acquisition and higher overdraft and account analysis fees.

For the nine months ended September 30, 2017, service charges on deposits accounts increased $50 million, or 22.9%, from the first nine months of 2016. This increase was primarily due to the full year-to-date impact of the First Niagara acquisition.

Cards and payments income

Cards and payments income, which consists of debit card, consumer and commercial credit card, and merchant services income, increased $9 million, or 13.6%, from the year-ago quarter. This increase was primarily due to the full-quarter impact of the First Niagara acquisition and our 2017 acquisition of Key Merchant Services, LLC, which increased merchant services fees compared to the same period one year ago.

For the nine months ended September 30, 2017, cards and payments income was $210 million, an increase of $46 million, or 28.0%, from the same period one year ago. This increase was primarily due to the full year-to-date impact of the First Niagara acquisition and our 2017 acquisition of Key Merchant Services, LLC.

Table of Contents

Other income

Other income, which consists primarily of gains on sales of loans held for sale, other service charges, and certain dealer trading income, was up $10 million, or 125.0%, from the year-ago quarter. This increase was primarily attributable to higher recoveries of loans that were charged-off by First Niagara prior to acquisition and gains on sales of loans held for sale.

For the nine months ended September 30, 2017, other income was up $73 million, or 119.7%, from the same period one year ago. This increase was driven by a $64 million one-time gain related to our Key Merchant Services, LLC acquisition that occurred in the second quarter of 2017 and recoveries of loans that were charged-off by First Niagara prior to acquisition, partially offset by lower trading income.

Noninterest expense

As shown in Figure 11, noninterest expense was $992 million for the third quarter of 2017 compared to $1.1 billion for the third quarter of 2016. The third quarter of 2017 included $36 million of merger-related charges compared to $189 million for the third quarter of 2016.

For the nine months ended September 30, 2017, noninterest expense was $3.0 billion compared to $2.5 billion for the same period one year ago. Merger-related charges for the nine months ended September 30, 2017, were $161 million compared to $258 million for the same period one year ago.

Figure 11. Noninterest Expense

	Three months ended September 30,		Change		Nine months ended September 30,		Change	
dollars in millions	2017	2016	Amount	Percent	2017	2016	Amount	Percent
Personnel [(a)]	$558	$594	$(36)	(6.1)%	$1,665	$1,425	$240	16.8 %
Net occupancy	74	73	1	1.4	239	193	46	23.8
Computer processing	56	70	(14)	(20.0)	171	158	13	8.2
Business services and professional fees	49	76	(27)	(35.5)	140	157	(17)	(10.8)
Equipment	29	26	3	11.5	83	68	15	22.1
Operating lease expense	24	15	9	60.0	64	42	22	52.4
Marketing	34	32	2	6.3	85	66	19	28.8
FDIC assessment	21	21	—	—	62	38	24	63.2
Intangible asset amortization	25	13	12	92.3	69	28	41	146.4
OREO expense, net	3	3	—	—	8	6	2	33.3
Other expense	119	159	(40)	(25.2)	414	355	59	16.6
Total noninterest expense	$992	$1,082	$(90)	(8.3)%	$3,000	$2,536	$464	18.3 %
Merger-related charges [(b)]	36	189	(153)	(81.0)	161	258	(97)	(37.6)
Total noninterest expense excluding merger-related charges [(c)]	$956	$893	$63	7.1 %	$2,839	$2,278	$561	24.6 %
Average full-time equivalent employees [(d)]	18,548	17,079	1,469	8.6 %	18,427	14,642	3,785	25.9 %

(a) Additional detail provided in Figure 13 entitled "Personnel Expense."

(b) Additional detail provided in Figure 12 entitled “Merger-Related Charges.”
(c) Non-GAAP measure.
(d) The number of average full-time equivalent employees has not been adjusted for discontinued operations.

Table of Contents

Figure 12. Merger-Related Charges

dollars in millions	Three months ended September 30, 2017	2016	Change Amount	Change Percent	Nine months ended September 30, 2017	2016	Change Amount	Change Percent
Net interest income	—	$(6)	$6	N/M	—	$(6)	$6	N/M
Operating lease income and other leasing gains	—	(2)	2	N/M	—	(2)	2	N/M
Other income	—	(10)	10	N/M	—	(10)	10	N/M
Noninterest income	—	(12)	12	N/M	—	(12)	12	N/M
Personnel	$25	97	(72)	(74.2)%	$86	148	$(62)	(41.9)%
Net occupancy	(2)	—	(2)	N/M	2	—	2	N/M
Business services and professional fees	2	32	(30)	(93.8)	13	44	(31)	(70.5)
Computer processing	4	15	(11)	(73.3)	11	15	(4)	(26.7)
Marketing	5	9	(4)	(44.4)	17	13	4	30.8
Other nonpersonnel expense	2	36	(34)	(94.4)	32	38	(6)	(15.8)
Noninterest expense	36	189	(153)	(81.0)	161	258	(97)	(37.6)
Total merger-related charges	$36	$207	$(171)	(82.6)%	$161	$276	$(115)	(41.7)%

Personnel

As shown in Figure 13, personnel expense, the largest category of our noninterest expense, decreased by $36 million, or 6.1%, for the third quarter of 2017 compared to the year-ago quarter. This decrease was primarily driven by lower severance expense as a result of the First Niagara acquisition in the third quarter of 2016. Personnel expenses were also down due to lower incentive and stock-based compensation due to strong capital market conditions in the year-ago period. Partially offsetting these declines was an increase in employee benefits expense due to the full-quarter impact of the First Niagara acquisition.

For the nine months ended September 30, 2017, personnel expense was up $240 million, or 16.8%, from the first nine months of 2016. This increase was primarily driven by the full year-to-date impact of the First Niagara acquisition and higher incentive and stock-based compensation related to stronger overall capital markets performance during the first nine months of 2017.

Figure 13. Personnel Expense

dollars in millions	Three months ended September 30, 2017	2016	Change Amount	Change Percent	Nine months ended September 30, 2017	2016	Change Amount	Change Percent
Salaries and contract labor	$339	$329	$10	3.0 %	$995	$839	$156	18.6 %
Incentive and stock-based compensation	134	162	(28)	(17.3)	398	352	46	13.1
Employee benefits	80	73	7	9.6	252	199	53	26.6
Severance	5	30	(25)	(83.3)	20	35	(15)	(42.9)
Total personnel expense	$558	$594	$(36)	(6.1)%	$1,665	$1,425	$240	16.8 %

Merger-related charges	25	97	(72)	(74.2)	86	148	(62)	(41.9)
Total personnel expense excluding merger-related charges	$533	$497	$36	7.2 %	$1,579	$1,277	$302	23.6 %

Net occupancy

Net occupancy expense increased $1 million, or 1.4%, for the third quarter of 2017, compared to the same period one year ago. This increase was primarily due to higher rental expenses as a result of the increase in occupied premises from the First Niagara acquisition, partially offset by lower expenses related to vacating leased properties prior to the end of the lease term.

For the nine months ended September 30, 2017, net occupancy expense increased $46 million, or 23.8%, from the nine months ended September 30, 2016, primarily due to an increase in various net occupancy expenses resulting from the First Niagara acquisition.

Other expense

Other expense comprises various miscellaneous expense items. The $40 million, or 25.2%, decrease in the current quarter compared to the same period one year ago reflects a charitable contribution made in accordance with Key's

Table of Contents

previously announced National Community Benefits Plan during the third quarter of 2016. The decrease in other expense is also attributable to lower other miscellaneous expenses.

For the nine months ended September 30, 2017, other expense increased $59 million, or 16.6%, from the nine months ended September 30, 2016, primarily due to the full year-to-date impact of the First Niagara acquisition.

Income taxes

We recorded tax expense from continuing operations of $134 million for the third quarter of 2017 and $16 million for the third quarter of 2016. For the nine months ended September 30, 2017, we recorded tax expense from continuing operations of $386 million, compared to $141 million for the same period one year ago.

Our federal tax expense (benefit) differs from the amount that would be calculated using the federal statutory tax rate, primarily because we generate income from investments in tax-advantaged assets, such as corporate-owned life insurance and credits associated with renewable energy and low-income housing investments, and make periodic adjustments to our tax reserves. Tax expense for the three months ended September 30, 2017, and September 30, 2016, was affected by net discrete income tax benefits of $13 million and detriments of $7 million, respectively. The tax expense for the third quarter of 2017 was also impacted due to merger-related charges of $36 million. Excluding those expenses, the tax expense for the third quarter of 2017 was $143 million.

Additional information pertaining to how our tax expense (benefit) and the resulting effective tax rates were derived is included in Note 13 ("Income Taxes") beginning on page 170 of our 2016 Form 10-K.

Line of Business Results

This section summarizes the financial performance of our two major business segments (operating segments): Key Community Bank and Key Corporate Bank. Note 19 ("Line of Business Results") describes the products and services offered by each of these business segments, provides more detailed financial information pertaining to the segments, and explains "Other Segments" and "Reconciling Items."

Figure 14 summarizes the contribution made by each major business segment to our "taxable-equivalent revenue from continuing operations" and "income (loss) from continuing operations attributable to Key" for the three- and nine-month periods ended September 30, 2017, and September 30, 2016.

Figure 14. Major Business Segments — Taxable-Equivalent Revenue from Continuing Operations and Income (Loss) from Continuing Operations Attributable to Key

	Three months ended September 30,		Change		Nine months ended September 30,		Change	
dollars in millions	2017	2016	Amount	Percent	2017	2016	Amount	Percent
REVENUE FROM CONTINUING OPERATIONS (TE)								
Key Community Bank	$959	$783	$176	22.5 %	$2,874	$1,976	$898	45.4 %
Key Corporate Bank	560	556	4	0.7	1,734	1,432	302	21.1
Other Segments	30	16	14	87.5	94	68	26	38.2
Total Segments	1,549	1,355	194	14.3	4,702	3,476	1,226	35.3
Reconciling Items [(a)]	5	(18)	23	N/M	(2)	(18)	16	N/M
Total	$1,554	$1,337	$217	16.2 %	$4,700	$3,458	$1,242	35.9 %

INCOME (LOSS) FROM CONTINUING OPERATIONS ATTRIBUTABLE TO KEY								
Key Community Bank	$161	$97	$64	66.0 %	$503	$259	$244	94.2 %
Key Corporate Bank	190	160	30	18.8	593	404	189	46.8
Other Segments	23	16	7	43.8	72	55	17	30.9
Total Segments	374	273	101	37.0	1,168	718	450	62.7
Reconciling Items [(a)]	(11)	(102)	91	N/M	(74)	(161)	87	N/M
Total	$363	$171	$192	112.3 %	$1,094	$557	$537	96.4 %

(a) Reconciling items consist primarily of the unallocated portion of merger-related charges and items not allocated to the business segments because they do not reflect their normal operations.

27

Table of Contents

Key Community Bank summary of operations

- Positive operating leverage compared to prior year
- Net income increased $64 million, or 66%, from prior year
- Average commercial and industrial loans increased $2.7 billion, or 17.2%, from the prior year
- Average deposits increased $10.2 billion, or 14.6%, from the prior year

As shown in Figure 15, Key Community Bank recorded net income attributable to Key of $161 million for the third quarter of 2017, compared to $97 million for the year-ago quarter, benefiting from momentum in Key's core businesses, as well as the full-quarter impact of the First Niagara acquisition.

TE net interest income increased by $137 million, or 25.7%, from the third quarter of 2016. The increase was primarily attributable to the full-quarter impact of the First Niagara acquisition, as well as the benefit from higher interest rates. Average loans and leases increased $6 billion, or 14.6%, largely driven by a $2.7 billion, or 17.2%, increase in commercial and industrial loans. Additionally, average deposits increased $10.2 billion, or 14.6%, from one year ago.

Noninterest income was up $39 million, or 15.6%, from the year-ago quarter, driven by the full quarter impact of the First Niagara acquisition. Strength in cards and payments, which includes the full-quarter impact of Key’s merchant services acquisition in the second quarter of 2017, and higher assets under management from market growth also contributed to the increase.

The provision for credit losses increased by $20 million, or 51.3%, and net loan charge-offs increased $10 million from the third quarter of 2016, primarily related to the acquisition of First Niagara.

Noninterest expense increased by $53 million, or 9%, from the year-ago quarter, largely driven by the full-quarter impact of the First Niagara acquisition, as well as core business activity, ongoing investments, recent acquisitions and seasonal trends. Personnel expense increased $29 million, while non-personnel expense increased by $24 million, including higher marketing expense and higher intangible amortization expense.

Table of Contents

Figure 15. Key Community Bank

dollars in millions	Three months ended September 30, 2017	2016	Change Amount	Percent	Nine months ended September 30, 2017	2016	Change Amount	Percent
SUMMARY OF OPERATIONS								
Net interest income (TE)	$670	$533	$137	25.7 %	$1,973	$1,324	$649	49.0 %
Noninterest income	289	250	39	15.6	901	652	249	38.2
Total revenue (TE)	959	783	176	22.5	2,874	1,976	898	45.4
Provision for credit losses	59	39	20	51.3	152	92	60	65.2
Noninterest expense	643	590	53	9.0	1,921	1,471	450	30.6
Income (loss) before income taxes (TE)	257	154	103	66.9	801	413	388	93.9
Allocated income taxes (benefit) and TE adjustments	96	57	39	68.4	298	154	144	93.5
Net income (loss) attributable to Key	$161	$97	$64	66.0 %	$503	$259	$244	94.2 %
AVERAGE BALANCES								
Loans and leases	$47,595	$41,548	$6,047	14.6 %	$47,376	$34,450	$12,926	37.5 %
Total assets	51,708	44,218	7,490	16.9	51,421	36,707	14,714	40.1
Deposits	79,563	69,397	10,166	14.6	79,438	58,704	20,734	35.3
Assets under management at period end	$38,660	$36,752	$1,908	5.2 %	$38,660	$36,752	$1,908	5.2 %

ADDITIONAL KEY COMMUNITY BANK DATA

dollars in millions	Three months ended September 30, 2017	2016	Change Amount	Percent	Nine months ended September 30, 2017	2016	Change Amount	Percent
NONINTEREST INCOME								
Trust and investment services income	$101	$86	$15	17.4 %	$298	$232	$66	28.4 %
Services charges on deposit accounts	78	70	8	11.4	230	180	50	27.8
Cards and payments income	65	54	11	20.4	180	143	37	25.9
Other noninterest income	45	40	5	12.5	193	97	96	99.0
Total noninterest income	$289	$250	$39	15.6 %	$901	$652	$249	38.2 %
AVERAGE DEPOSITS OUTSTANDING								
NOW and money market deposit accounts	$44,481	$38,417	$6,064	15.8 %	$44,795	$32,685	$12,110	37.1 %
Savings deposits	5,165	4,369	796	18.2	5,242	3,030	2,212	73.0
Certificates of deposits ($100,000 or more)	4,195	2,606	1,589	61.0	4,031	2,371	1,660	70.0
Other time deposits	4,657	4,944	(287)	(5.8)	4,662	3,799	863	22.7
Noninterest-bearing deposits	21,065	19,061	2,004	10.5	20,708	16,819	3,889	23.1
Total deposits	$79,563	$69,397	$10,166	14.6 %	$79,438	$58,704	$20,734	35.3 %
HOME EQUITY LOANS								
Average balance	$12,182	$11,703						
Combined weighted-average loan-to-value ratio (at date of origination)	69 %	70 %						
Percent first lien positions	60	55						
OTHER DATA								
Branches	1,208	1,322						
Automated teller machines	1,588	1,701						

Key Corporate Bank summary of operations

• Positive operating leverage compared to prior year
• Net income up $30 million, or 18.8%, from prior year
• Average loan and lease balances up $3.5 billion, or 10.1%, from the prior year

As shown in Figure 16, Key Corporate Bank recorded net income attributable to Key of $190 million for the third quarter of 2017, compared to $160 million for the same period one year ago.

TE net interest income increased by $13 million, or 4.7%, compared to the third quarter of 2016. Average loan and lease balances increased $3.5 billion, or 10.1%, from the year-ago quarter, driven by growth in commercial and industrial and commercial mortgage loans. Average deposit balances decreased $1.1 billion, or 5.1%, from the year-ago quarter, driven by the managed exit of higher cost corporate and public sector deposits.

Noninterest income was down $9 million, or 3.2%, from the prior year. This decline was mostly due to lower investment banking and debt placement fees, resulting from weaker market conditions in the current quarter as

Table of Contents

compared to the prior year quarter. This decrease was partially offset by growth in mortgage servicing fees and corporate services income compared to the prior year.

During the third quarter of 2017, Key Corporate Bank benefited from a large recovery in the commercial and industrial portfolio, as well as improving credit quality in the overall portfolio. Accordingly, the provision for credit losses decreased $34 million, or 147.8%, compared to the third quarter of 2016, with $21 million less of net loan charge-offs.

Noninterest expense decreased by $7 million, or 2.3%, from the third quarter of 2016. The decrease from the prior year was largely driven by lower performance-based compensation. Slightly offsetting this decrease were higher levels of operating lease expense, business services and professional fees, and cards and payments expense.

Figure 16. Key Corporate Bank

	Three months ended September 30,		Change		Nine months ended September 30,		Change	
dollars in millions	2017	2016	Amount	Percent	2017	2016	Amount	Percent
SUMMARY OF OPERATIONS								
Net interest income (TE)	$291	$278	$13	4.7 %	$907	$716	$191	26.7 %
Noninterest income	269	278	(9)	(3.2)	827	716	111	15.5
Total revenue (TE)	560	556	4	0.7	1,734	1,432	302	21.1
Provision for credit losses	(11)	23	(34)	(147.8)	26	110	(84)	(76.4)
Noninterest expense	303	310	(7)	(2.3)	904	805	99	12.3
Income (loss) before income taxes (TE)	268	223	45	20.2	804	517	287	55.5
Allocated income taxes and TE adjustments	78	63	15	23.8	212	114	98	86.0
Net income (loss)	$190	$160	$30	18.8	$592	$403	$189	46.9
Less: Net income (loss) attributable to noncontrolling interests	—	—	—	—	(1)	(1)	—	—
Net income (loss) attributable to Key	$190	$160	$30	18.8 %	$593	$404	$189	46.8 %
AVERAGE BALANCES								
Loans and leases	$38,040	$34,561	$3,479	10.1 %	$37,823	$30,312	$7,511	24.8 %
Loans held for sale	1,521	1,103	418	37.9	1,208	836	372	44.5
Total assets	45,276	40,584	4,692	11.6	44,526	35,984	8,542	23.7
Deposits	21,559	22,708	(1,149)	(5.1)%	21,237	19,980	1,257	6.3 %

ADDITIONAL KEY CORPORATE BANK DATA

	Three months ended September 30,		Change		Nine months ended September 30,		Change	
dollars in millions	2017	2016	Amount	Percent	2017	2016	Amount	Percent
NONINTEREST INCOME								
Trust and investment services income	$34	$36	$(2)	(5.6)%	$106	$109	$(3)	(2.8)%
Investment banking and debt placement fees	137	153	(16)	(10.5)	394	317	77	24.3
Operating lease income and other leasing gains	13	10	3	30.0	56	38	18	47.4
Corporate services income	41	36	5	13.9	116	113	3	2.7
Service charges on deposit accounts	13	15	(2)	(13.3)	37	38	(1)	(2.6)

Cards and payments income	10	10	—	—	29	20	9	45.0
Payments and services income	64	61	3	4.9	182	171	11	6.4
Mortgage servicing fees	18	13	5	38.5	47	35	12	34.3
Other noninterest income	3	5	(2)	(40.0)	42	46	(4)	(8.7)
Total noninterest income	$269	$278	$(9)	(3.2)%	$827	$716	$111	15.5 %

Other Segments

Other Segments consist of Corporate Treasury, Key’s Principal Investing unit, and various exit portfolios. Other Segments generated net income attributable to Key of $23 million for the third quarter of 2017, compared to $16 million for the same period last year, driven by increases in operating lease income and other leasing gains and corporate-owned life insurance income.

Table of Contents

Financial Condition

Loans and loans held for sale

At September 30, 2017, total loans outstanding from continuing operations were $86.5 billion, compared to $86.0 billion at December 31, 2016. Loans related to the discontinued operations of the education lending business and excluded from total loans were $1.4 billion at September 30, 2017, and $1.6 billion at December 31, 2016. For more information on balance sheet carrying value, see Note 1 ("Summary of Significant Accounting Policies") under the headings "Loans" and "Loans Held for Sale" on page 107 of our 2016 Form 10-K.

During the second quarter of 2017, Key finalized the fair value of the First Niagara acquired loan portfolio, adjusting the discount from $548 million to $603 million. At September 30, 2017, $302 million of the fair value discount remained. For more information on the financial statement impact of the finalization of the First Niagara acquired loan portfolio, see Note 2 ("Business Combination").

Commercial loan portfolio

Commercial loans outstanding were $62.7 billion at September 30, 2017, an increase of $837 million, or 1.4%, compared to December 31, 2016, primarily driven by an increase in commercial and industrial loans. Figure 17 provides our commercial loan portfolios by industry classification at September 30, 2017, and December 31, 2016.

Figure 17. Commercial Loans by Industry

September 30, 2017 dollars in millions	Commercial and industrial	Commercial real estate	Commercial lease financing	Total commercial loans	Percent of total
Industry classification:					
Agricultural	$ 736	$ 165	$ 70	$ 971	1.5 %
Automotive	2,064	472	77	2,613	4.2
Business products	1,877	160	55	2,092	3.3
Business services	2,571	168	272	3,011	4.8
Commercial real estate	5,853	10,892	23	16,768	26.7
Construction materials and contractors	1,719	343	132	2,194	3.5
Consumer discretionary	3,769	558	455	4,782	7.6
Consumer services	2,965	1,034	260	4,259	6.8
Equipment	1,599	145	123	1,867	3.0
Financial	3,865	81	347	4,293	6.9
Healthcare	3,048	2,376	403	5,827	9.3
Materials manufacturing and mining	1,907	117	135	2,159	3.4
Media	418	23	46	487	.8
Oil and gas	1,062	19	50	1,131	1.8
Public exposure	2,430	58	979	3,467	5.5
Technology	535	3	9	547	.9
Transportation	1,424	246	906	2,576	4.1
Utilities	3,149	7	374	3,530	5.6
Other	156	16	—	172	.3
Total	$ 41,147	$ 16,883	$ 4,716	$ 62,746	100.0 %

December 31, 2016 dollars in millions	Commercial and	Commercial real estate	Commercial lease financing	Total commercial loans	Percent of total

	industrial				
Industry classification:					
Agricultural	$ 844	$ 194	$ 151	$ 1,189	1.9 %
Automotive	2,139	491	74	2,704	4.4
Business products	1,243	152	31	1,426	2.3
Business services	2,648	179	303	3,130	5.1
Commercial real estate	4,759	11,235	2	15,996	25.8
Construction materials and contractors	1,282	307	79	1,668	2.7
Consumer discretionary	3,367	539	314	4,220	6.8
Consumer services	2,281	749	66	3,096	5.0
Equipment	1,582	107	87	1,776	2.9
Financial	3,864	95	296	4,255	6.9
Healthcare	3,487	2,577	526	6,590	10.6
Materials manufacturing and mining	2,743	276	212	3,231	5.2
Media	478	18	70	566	.9
Oil and gas	1,094	27	62	1,183	1.9
Public exposure	2,621	311	1,204	4,136	6.7
Technology	485	6	34	525	.8
Transportation	940	148	923	2,011	3.3
Utilities	3,441	26	251	3,718	6.0
Other	470	19	—	489	.8
Total	$ 39,768	$ 17,456	$ 4,685	$ 61,909	100.0 %

31

Table of Contents

Commercial and industrial. Our commercial and industrial loans represented 48% of our total loan portfolio at September 30, 2017, and 46% at December 31, 2016, and are the largest component of our total loans. These loans are originated by both Key Corporate Bank and Key Community Bank and consist of fixed and variable rate loans to our large, middle market, and small business clients.

Commercial and industrial loans increased $1.4 billion, or 3.5%, from December 31, 2016, with Key Corporate Bank increasing $1.2 billion and Key Community Bank up $576 million. This growth was partially attributable to growth within our middle market segment driven by increased production and productivity partially offset by higher levels of paydowns.

Our largest commercial and industrial loan industry classification, commercial real estate, increased by 23.0%, when compared to December 31, 2016. We experienced growth in our business products, consumer services, and transportation commercial and industrial loan classifications, increasing 51.0%, 30.0%, and 51.5%, respectively, from December 31, 2016. Partially offsetting these increases, the materials manufacturing and mining and healthcare commercial and industrial loan classifications, which represented approximately 5% and 7%, respectively, of the commercial and industrial loan portfolio at September 30, 2017, decreased 30.5% and 12.6%, respectively, from December 31, 2016.

Commercial real estate loans. Our commercial real estate lending business is conducted through two primary sources: our 15-state banking franchise, and KeyBank Real Estate Capital, a national line of business that cultivates relationships with owners of commercial real estate located both within and beyond the branch system. This line of business deals primarily with nonowner-occupied properties (generally properties for which at least 50% of the debt service is provided by rental income from nonaffiliated third parties) and accounted for approximately 70% of our average year-to-date commercial real estate loans for the three months ended September 30, 2017, and 69% for the three months ended September 30, 2016. KeyBank Real Estate Capital generally focuses on larger owners and operators of commercial real estate.

Commercial real estate loans totaled $16.9 billion at September 30, 2017, and $17.5 billion at December 31, 2016, and represented 20% of our total loan portfolio at both September 30, 2017, and December 31, 2016. The $573 million decrease from December 31, 2016, was due to an increase in paydowns in our real estate — commercial mortgage loan portfolio and the planned reduction of certain acquired loans. Commercial real estate loans were also negatively impacted by clients continuing to take advantage of attractive capital markets alternatives. These loans, which include both owner- and nonowner-occupied properties, represented 27% of our commercial loan portfolio at September 30, 2017, and 28% at December 31, 2016.

Figure 18 includes commercial mortgage and construction loans in both Key Community Bank and Key Corporate Bank. As shown in Figure 18, this loan portfolio is diversified by both property type and geographic location of the underlying collateral.

As presented in Figure 18, at September 30, 2017, our commercial real estate portfolio included commercial mortgage loans of $14.9 billion and construction loans of $2.0 billion, representing 17% and 2%, respectively, of our total loans. At September 30, 2017, nonowner-occupied loans represented 15% of our total loans and owner-occupied loans represented 4% of our total loans.

Also shown in Figure 18, 79% of our commercial real estate loans at September 30, 2017, were for nonowner-occupied properties compared to 78% at December 31, 2016. Approximately 14% of these loans were construction loans at September 30, 2017, and 17% were construction loans at December 31, 2016.

Table of Contents

Figure 18. Commercial Real Estate Loans

dollars in millions	Geographic Region [a] West	Southwest	Central	Midwest	Southeast	Northeast	National	Total	Percent of Total	Construction	Commercial Mortgage
September 30, 2017											
Nonowner-occupied:											
Retail properties	$198	$126	$123	$216	$250	$866	$242	$2,021	12.0 %	$217	$1,804
Multifamily properties	356	216	675	527	1,097	2,128	140	5,139	30.4	1,096	4,043
Health facilities	212	—	350	191	282	1,060	142	2,237	13.3	110	2,127
Office buildings	183	10	97	145	218	1,029	31	1,713	10.2	131	1,582
Warehouses	99	21	33	105	142	377	37	814	4.8	44	770
Manufacturing facilities	15	—	21	33	14	74	36	193	1.1	30	163
Hotels/Motels	14	—	86	4	10	197	30	341	2.0	39	302
Residential properties	1	—	—	1	2	188	—	192	1.1	79	113
Land and development	22	—	5	2	8	73	—	110	.7	75	35
Other	47	—	26	85	12	340	70	580	3.4	19	561
Total nonowner-occupied	1,147	373	1,416	1,309	2,035	6,332	728	13,340	79.0	1,840	11,500
Owner-occupied	942	4	270	541	122	1,664	—	3,543	21.0	114	3,429
Total	$2,089	$377	$1,686	$1,850	$2,157	$7,996	$728	16,883	100.0 %	$1,954	$14,929
December 31, 2016											
Total	$2,032	$291	$1,508	$2,281	$2,304	$8,340	$700	$17,456		$2,345	$15,111
September 30, 2017											
Nonowner-occupied:											
Nonperforming loans	—	—	—	$5	$9	$7	—	$21	N/M	—	$21
Accruing loans past due 90 days or more	$1	—	—	—	3	19	—	23	N/M	—	22
Accruing loans past due 30 through 89 days	5	—	—	2	7	55	—	69	N/M	$20	49

(a)Regions are defined as follows

West –	Alaska, California, Hawaii, Idaho, Montana, Oregon, Washington, and Wyoming
Southwest –	Arizona, Nevada, and New Mexico
Central –	Arkansas, Colorado, Oklahoma, Texas, and Utah
Midwest –	Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, and Wisconsin
Southeast –	Alabama, Delaware, Florida, Georgia, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, Washington D.C., and West Virginia
Northeast –	Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, and Vermont
National –	Accounts in three or more regions

Nonperforming loans related to nonowner-occupied properties decreased by $1 million from December 31, 2016, to $21 million at September 30, 2017. Our nonowner-occupied commercial real estate portfolio has decreased by 2.3%, or $321 million, since December 31, 2016. The decline reflects overall business activity and payoffs in our KeyBank Real Estate Capital line of business.

Commercial TDRs

We modify and extend certain commercial loans in the normal course of business for our clients. Loan modifications vary and are handled on a case-by-case basis with strategies responsive to the specific circumstances of each loan and borrower. In many cases, borrowers have other resources and can reinforce the credit with additional capital, collateral, guarantees, or other income sources. For more information on concession types for our commercial accruing and nonaccruing TDRs, see Note 5 (“Asset Quality”), and the section titled “Loans and loans held for sale” in Part II, Item 7. “Management’s Discussion and Analysis of Financial Condition and Results of Operations” on page 57 of our 2016 Form 10-K.

Figure 19. Commercial TDRs by Accrual Status

in millions	September 30, 2017	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016
Commercial TDRs by Accrual Status					
Nonaccruing	$ 95	$ 106	$ 70	$ 51	$ 67
Accruing	13	18	16	16	18
Total Commercial TDRs	$ 108	$ 124	$ 86	$ 67	$ 85

Table of Contents

Consumer loan portfolio

Consumer loans outstanding decreased by $383 million, or 1.6%, from December 31, 2016, mostly related to continued decline in the home equity loan portfolio, largely the result of pay downs on home equity lines of credit and term loans. This decrease was partially offset by an increase in auto loans.

The home equity portfolio is the largest segment of our consumer loan portfolio. Approximately 99% of this portfolio at September 30, 2017, was originated from our Key Community Bank within our 15-state footprint.

As shown in Figure 15, we held the first lien position for approximately 60% of the Key Community Bank home equity portfolio at September 30, 2017, and 55% at September 30, 2016. At September 30, 2017, 40% of the Key Community Bank home equity portfolio was secured by second lien mortgages. For consumer loans with real estate collateral, we track borrower performance monthly. Regardless of the lien position, credit metrics are refreshed quarterly, including recent FICO scores as well as original and updated loan-to-value ratios. This information is used in establishing the ALLL. Our methodology is described in Note 1 ("Summary of Significant Accounting Policies") under the heading "Allowance for Loan and Lease Losses" beginning on page 109 of our 2016 Form 10-K.

Loan sales

As shown in Figure 20, during the first nine months of 2017, we sold $8.1 billion of loans. Sales of loans classified as held for sale generated net gains of $111 million in the first nine months of 2017 and are included in "investment banking and debt placement fees" and "other income" on the income statement.

Among the factors that we consider in determining which loans to sell are:

- our business strategy for particular lending areas;
- whether particular lending businesses meet established performance standards or fit with our relationship banking strategy;
- our A/LM needs;
- the cost of alternative funding sources;
- the level of credit risk;
- capital requirements; and
- market conditions and pricing.

Figure 20 summarizes our loan sales for the first nine months of 2017 and all of 2016.

Figure 20. Loans Sold (Including Loans Held for Sale)

in millions	Commercial	Commercial Real Estate	Commercial Lease Financing	Residential Real Estate	Total
2017					
Third quarter	$ 337	$ 2,534	$ 93	$ 279	$3,243
Second quarter	205	2,097	14	230	2,546
First quarter	49	2,011	83	194	2,337
Total	$ 591	$ 6,642	$ 190	$ 703	$8,126
2016					
Fourth quarter	$ 83	$ 2,521	$ 93	$ 232	$2,929
Third quarter	105	1,791	52	260	2,208
Second quarter	83	1,518	121	111	1,833

First quarter	46	925	88	89	1,148
Total	$ 317	$ 6,755	$ 354	$ 692	$8,118

Table of Contents

Figure 21 shows loans that are either administered or serviced by us, but not recorded on the balance sheet; this includes loans that were sold.

Figure 21. Loans Administered or Serviced

in millions	September 30, 2017	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016
Commercial real estate loans	$ 224,361	$ 218,667	$ 218,387	$ 218,135	$ 213,998
Residential mortgage	4,458	4,345	4,272	4,198	—
Education loans	974	1,019	1,067	1,122	1,172
Commercial lease financing	856	833	916	899	930
Commercial loans	458	446	427	418	1,461
Total	$ 231,107	$ 225,310	$ 225,069	$ 224,772	$ 217,561

In the event of default by a borrower, we are subject to recourse with respect to approximately $3.0 billion of the $231.1 billion of loans administered or serviced at September 30, 2017. Additional information about this recourse arrangement is included in Note 16 (“Contingent Liabilities and Guarantees”) under the heading “Recourse agreement with FNMA.”

We derive income from several sources when retaining the right to administer or service loans that are sold. We earn noninterest income (recorded as “mortgage servicing fees”) from fees for servicing or administering loans. This fee income is reduced by the amortization of related servicing assets. In addition, we earn interest income from investing funds generated by escrow deposits collected in connection with the servicing of commercial real estate loans.

Securities

Our securities portfolio totaled $29.3 billion at September 30, 2017, compared to $30.4 billion at December 31, 2016. Available-for-sale securities were $19.0 billion at September 30, 2017, compared to $20.2 billion at December 31, 2016. Held-to-maturity securities were $10.3 billion at September 30, 2017, and $10.2 billion at December 31, 2016.

As shown in Figure 22, all of our mortgage-backed securities, which include both securities available for sale and held-to-maturity securities, are issued by government-sponsored enterprises or GNMA and traded in liquid secondary markets. These securities are recorded on the balance sheet at fair value for the available-for-sale portfolio and at cost for the held-to-maturity portfolio. For more information about these securities, see Note 6 (“Fair Value Measurements”) under the heading “Qualitative Disclosures of Valuation Techniques,” and Note 7 (“Securities”).

Figure 22. Mortgage-Backed Securities by Issuer

in millions	September 30, 2017	December 31, 2016
FHLMC	$ 6,178	$ 6,415
FNMA	9,639	9,879
GNMA	13,268	13,920
Total [(a)]	$ 29,085	$ 30,214

(a) Includes securities held in the available-for-sale and held-to-maturity portfolios.

Securities available for sale

The majority of our securities available for sale portfolio consists of federal agency CMOs and mortgage-backed securities. CMOs are debt securities secured by a pool of mortgages. These mortgage securities generate interest income, serve as collateral to support certain pledging agreements, and provide liquidity value under regulatory requirements. At September 30, 2017, we had $18.8 billion invested in CMOs and other mortgage-backed securities in the available-for-sale portfolio, compared to $20.0 billion at December 31, 2016.

We periodically evaluate our securities available for sale portfolio in light of established A/LM objectives, changing market conditions that could affect the profitability of the portfolio, the regulatory environment, and the level of interest rate risk to which we are exposed. These evaluations may cause us to take steps to adjust our overall balance sheet positioning.

Table of Contents

In addition, the size and composition of our securities available for sale portfolio could vary with our needs for liquidity and the extent to which we are required (or elect) to hold these assets as collateral to secure public funds and trust deposits. Although we generally use debt securities for this purpose, other assets, such as securities purchased under resale agreements or letters of credit, are used occasionally when they provide a lower cost of collateral or more favorable risk profiles.

Our investing activities continue to complement other balance sheet developments and provide for our ongoing liquidity management needs. Our actions to not reinvest the monthly security cash flows at various times provide the liquidity necessary to address our funding requirements. These funding requirements include ongoing loan growth and occasional debt maturities. At other times, we may make additional investments that go beyond the replacement of maturities or mortgage security cash flows as our liquidity position and/or interest rate risk management strategies may require. Lastly, our focus on investing in high quality liquid assets, including GNMA securities, is related to liquidity management strategies to satisfy regulatory requirements.

Figure 23 shows the composition, yields, and remaining maturities of our securities available for sale. For more information about these securities, including gross unrealized gains and losses by type of security and securities pledged, see Note 7 ("Securities").

Figure 23. Securities Available for Sale

dollars in millions	U.S. Treasury, Agencies, and Corporations	States and Political Subdivisions	Agency Residential Collateralized Mortgage Obligations [(a)]	Agency Residential Mortgage-backed Securities [(a)]	Agency Commercial Mortgage-backed Securities	Other Securities [(b)]	Total	Weighted-Average Yield [(c)]
September 30, 2017								
Remaining maturity:								
One year or less	$ 9	$ 3	$ 162	$ 18	—	—	$ 192	2.94 %
After one through five years	58	7	12,464	1,482	$ 1,794	$ 20	15,825	2.05
After five through ten years	90	—	2,775	32	88	—	2,985	1.92
After ten years	1	—	—	9	—	—	10	3.29
Fair value	$ 158	$ 10	$ 15,401	$ 1,541	$ 1,882	$ 20	$ 19,012	—
Amortized cost	160	10	15,580	1,547	1,928	17	19,242	2.04 %
Weighted-average yield [(c)]	1.76 %	6.26 %	2.01 %	2.09 %	2.23 %	— [(d)]	2.04 % [(d)]	—
Weighted-average maturity	4.4 years	1.9 years	4.0 years	3.8 years	3.8 years	3.1 years	3.9 years	—
December 31, 2016								
Fair value	$ 184	$ 11	$ 16,408	$ 1,846	$ 1,743	$ 20	$ 20,212	—
Amortized cost	188	11	16,652	1,857	1,778	21	20,507	2.00 %

(a) Maturity is based upon expected average lives rather than contractual terms.

(b) Includes primarily marketable equity securities.

(c) Weighted-average yields are calculated based on amortized cost. Such yields have been adjusted to a TE basis using the statutory federal income tax rate of 35%.

(d) Excludes $20 million of securities at September 30, 2017, that have no stated yield.

Held-to-maturity securities

Federal agency CMOs and mortgage-backed securities constitute essentially all of our held-to-maturity securities. The remaining balance comprises primarily foreign bonds. Figure 24 shows the composition, yields, and remaining maturities of these securities.

Table of Contents

Figure 24. Held-to-Maturity Securities

dollars in millions	Agency Residential Collateralized Mortgage Obligations	Agency Residential Mortgage-backed Securities	Agency Commercial Mortgage-backed Securities	Other Securities	Total	Weighted-Average Yield [a]
September 30, 2017						
Remaining maturity:						
One year or less	$ 73	—	—	3	$76	2.34 %
After one through five years	6,804	—	$ 690	$ 12	7,506	2.02
After five through ten years	911	$ 601	575	—	2,087	2.42
After ten years	—	—	607	—	607	2.66
Amortized cost	$ 7,788	$ 601	$ 1,872	$ 15	$10,276	2.14 %
Fair value	7,647	600	1,847	15	10,109	—
Weighted-average yield	1.96 %	2.68 %	2.71 %	2.85 %	2.14 %	—
Weighted-average maturity	3.8 years	6.5 years	7.4 years	1.9 years	4.6 years	—
December 31, 2016						
Amortized cost	$ 8,404	$ 629	$ 1,184	$ 15	$10,232	2.05 %
Fair value	8,232	624	1,136	15	10,007	—

(a) Weighted-average yields are calculated based on amortized cost. Such yields have been adjusted to a TE basis using the statutory federal income tax rate of 35%.

Other investments

Principal investments — investments in equity and debt instruments made by our principal investing unit — represented 21% of other investments at September 30, 2017, and 25% at December 31, 2016. They include direct investments (investments made in a particular company) as well as indirect investments (investments made through funds that include other investors). Principal investments are predominantly made in privately held companies and are carried at fair value. The fair value of the direct investments was $13 million at September 30, 2017, and $27 million at December 31, 2016, while the fair value of the indirect investments was $138 million at September 30, 2017, and $158 million at December 31, 2016. Under the requirements of the Volcker Rule, we will be required to dispose of some or all of our indirect principal investments. On January 13, 2017, Key filed for an additional extension for illiquid funds, to retain certain indirect investments until the earlier of the date on which the investment is conformed or is expected to mature, or July 21, 2022. The application for an extension was approved on February 14, 2017. As of September 30, 2017, we have not committed to a plan to sell these investments, therefore, these investments continue to be valued using the net asset value per share methodology. For more information about the Volcker Rule, see the discussion in Item 1 under the heading "Other Regulatory Developments under the Dodd-Frank Act — 'Volcker Rule'" in the section entitled "Supervision and Regulation" beginning on page 16 of our 2016 Form 10-K.

Most of our other investments are not traded on an active market. We determine the fair value at which these investments should be recorded based on the nature of the specific investment and all available relevant information. This review may encompass such factors as the issuer's past financial performance and future potential, the values of public companies in comparable businesses, the risks associated with the particular business or investment type, current market conditions, the nature and duration of resale restrictions, the issuer's payment history, our knowledge of the industry, third-party data, and other relevant factors. During the first nine months of 2017, net gains from our principal investing activities (including results attributable to noncontrolling interests) totaled $4 million, which includes $9 million of net unrealized losses. These net gains are recorded as "net gains (losses) from principal investing" on the income statement. Additional information regarding these investments is provided in Note 6 ("Fair Value

Measurements”).

Deposits and other sources of funds

Domestic deposits are our primary source of funding. The composition of our average deposits is shown in Figure 7 in the section entitled “Net interest income.” During the third quarter of 2017, average deposits totaled $103.1 billion, an increase of $8.2 billion compared to the year-ago quarter, primarily reflecting a full-quarter impact of the First Niagara acquisition and core retail and commercial deposit growth.

Wholesale funds, consisting of short-term borrowings, averaged $1.3 billion during the third quarter of 2017, compared to $1.8 billion during the third quarter of 2016. The change from the third quarter of 2016 was caused by decreases of $122 million in federal funds purchased and securities sold under repurchase agreements, and $321 million in bank notes and other short-term borrowings.

Table of Contents

Capital

At September 30, 2017, our shareholders’ equity was $15.2 billion, up $9 million from December 31, 2016. The following sections discuss certain factors that contributed to this change. For other factors that contributed to the change, see the Consolidated Statements of Changes in Equity and Note 18 (“Shareholders' Equity”).

CCAR, capital actions, and dividends

As part of its ongoing supervisory process, the Federal Reserve requires BHCs like KeyCorp to submit an annual comprehensive capital plan and to update that plan to reflect material changes in the BHC’s risk profile, business strategies, or corporate structure, including but not limited to changes in planned capital actions. Consistent with our 2017 capital plan, we paid a quarterly dividend of $.095 per Common Share, which equated to $102 million for the third quarter of 2017. We made payments of $12.50 per depository share on the depositary shares related to our Series D Preferred Stock during the third quarter of 2017, for a total of $7 million. We made payments of $.382813 per depositary share on the depositary shares related to our Series E Preferred Stock during the third quarter of 2017, for a total of $8 million.

Further information regarding the capital planning process and CCAR is included under the heading “Capital planning and stress testing” in the “Supervision and Regulation” section beginning on page 12 of our 2016 Form 10-K. For more information on our 2017 capital plan actions, see Note 18 (“Shareholders' Equity “).

Common shares outstanding

Our Common Shares are traded on the NYSE under the symbol KEY with 38,839 holders of record at September 30, 2017. Our book value per Common Share was $13.18 based on 1.079 billion shares outstanding at September 30, 2017, compared to $12.58 per Common Share based on 1.079 billion shares outstanding at December 31, 2016. At September 30, 2017, our tangible book value per Common Share was $10.52, compared to $9.99 per Common Share at December 31, 2016.

Figure 25 shows activities that caused the change in outstanding common shares over the past five quarters.

Figure 25. Changes in Common Shares Outstanding

	2017			2016	
in thousands	Third	Second	First	Fourth	Third
Shares outstanding at beginning of period	1,092,739	1,097,479	1,079,314	1,082,055	842,703
Open market repurchases and return of shares under employee compensation plans	(15,298)	(5,072)	(8,673)	(4,380)	(5,240)
Shares issued under employee compensation plans (net of cancellations)	1,598	332	6,270	1,642	4,857
Series A Preferred Stock exchanged for common shares	—	—	20,568	—	—
Common shares issued to acquire First Niagara	—	—	—	(3)	239,735
Shares outstanding at end of period	1,079,039	1,092,739	1,097,479	1,079,314	1,082,055

As shown above, Common Shares outstanding decreased by 13.7 million shares during the third quarter of 2017. This decrease was primarily due to common share repurchases under our 2017 capital plan.

At September 30, 2017, we had 177.7 million treasury shares, compared to 177.4 million treasury shares at December 31, 2016. Going forward we expect to reissue treasury shares as needed in connection with stock-based compensation awards and for other corporate purposes.

Information on repurchases of Common Shares by KeyCorp is included in Part II, Item 2. “Unregistered Sales of Equity Securities and Use of Proceeds” of this report.

Table of Contents

Capital adequacy

Capital adequacy is an important indicator of financial stability and performance. All of KeyCorp's capital ratios remained in excess of regulatory requirements at September 30, 2017. Our capital and liquidity levels are intended to position us to weather an adverse economic cycle while continuing to serve our clients' needs, as well as to meet the Regulatory Capital Rules described in the "Supervision and regulation" section of Item 2 of this report. Our shareholders' equity to assets ratio was 11.15% at September 30, 2017, compared to 11.17% at December 31, 2016. Our tangible common equity to tangible assets ratio was 8.49% at September 30, 2017, compared to 8.09% at December 31, 2016.

The capital modifications mandated by the Regulatory Capital Rules, which became effective on January 1, 2015, for KeyCorp, require higher and better-quality capital and introduced a new capital measure, "Common Equity Tier 1." The Rules phased out the treatment of certain capital securities and cumulative preferred securities as eligible Tier 1 capital. The phase-out period, which began January 1, 2015, for "standardized approach" banking organizations such as KeyCorp, resulted in our trust preferred securities issued by the KeyCorp capital trusts and acquired from First Niagara, being treated only as Tier 2 capital starting in 2016. The new minimum capital and leverage ratios under the Regulatory Capital Rules, together with the estimated ratios of KeyCorp at September 30, 2017, calculated on a fully phased-in basis, are set forth under the heading "New minimum capital and leverage ratio requirements" in the "Supervision and regulation" section in Item 2 of this report. Beginning with the implementation of the Regulatory Capital Rules, deferred tax assets that arise from net operating loss and tax credit carryforwards are deductible from Common Equity Tier 1 on a phase-in basis.

As of January 1, 2016, KeyCorp (and its banking subsidiaries) were each required to maintain, on a consolidated basis, a minimum Common Equity Tier 1 capital ratio of 4.5%, Tier 1 risk-based capital ratio of 6.0%, a total risk-based capital ratio of 8.0%, and a Tier 1 leverage ratio of 4.0%. Figure 26 presents our risk based capital ratios and more detail on our capital components at September 30, 2017, and December 31, 2016. Information regarding the regulatory capital ratios of KeyCorp's banking subsidiaries is presented annually, in Note 23 ("Shareholders' Equity") beginning on page 198 of our 2016 Form 10-K.

Table of Contents

Figure 26. Capital Components and Risk-Weighted Assets

dollars in millions	September 30, 2017	December 31, 2016
COMMON EQUITY TIER 1		
Key shareholders' equity (GAAP)	$15,249	$15,240
Less: Preferred Stock [a]	1,009	1,640
Common Equity Tier 1 capital before adjustments and deductions	14,240	13,600
Less: Goodwill, net of deferred taxes	2,427	2,405
Intangible assets, net of deferred taxes	218	155
Deferred tax assets	9	4
Net unrealized gains (losses) on available-for-sale securities, net of deferred taxes	(145)	(185)
Accumulated gains (losses) on cash flow hedges, net of deferred taxes	(66)	(52)
Amounts in AOCI attributed to pension and postretirement benefit costs, net of deferred taxes	(332)	(339)
Total Common Equity Tier 1 capital	$12,129	$11,612
TIER 1 CAPITAL		
Common Equity Tier 1	$12,129	$11,612
Additional Tier 1 capital instruments and related surplus	1,009	1,640
Non-qualifying capital instruments subject to phase-out	—	—
Less: Deductions	2	3
Total Tier 1 capital	13,136	13,249
TIER 2 CAPITAL		
Tier 2 capital instruments and related surplus	1,381	1,450
Allowance for losses on loans and liability for losses on lending-related commitments [b]	956	939
Net unrealized gains on available-for-sale preferred stock classified as an equity security	—	—
Less: Deductions	—	—
Total Tier 2 capital	2,337	2,389
Total risk-based capital	$15,473	$15,638
RISK-WEIGHTED ASSETS		
Risk-weighted assets on balance sheet	$94,995	$94,959
Risk-weighted off-balance sheet exposure	22,311	25,848
Market risk-equivalent assets	927	864
Gross risk-weighted assets	118,233	121,671
Less: Excess allowance for loan and lease losses	—	—
Net risk-weighted assets	$118,233	$121,671
AVERAGE QUARTERLY TOTAL ASSETS	$133,631	$133,795
CAPITAL RATIOS		
Tier 1 risk-based capital	11.11 %	10.89 %
Total risk-based capital	13.09	12.85
Leverage [c]	9.83	9.90
Common Equity Tier 1	10.26	9.54

(a) Net of capital surplus.

(b) The ALLL included in Tier 2 capital is limited by regulation to 1.25% of the institution's standardized total risk-weighted assets (excluding its standardized market risk-weighted assets). The ALLL includes $18 million and $24 million of allowance classified as "discontinued assets" on the balance sheet at September 30, 2017, and December 31, 2016, respectively.

(c) This ratio is Tier 1 capital divided by average quarterly total assets as defined by the Federal Reserve less: (i) goodwill, (ii) the disallowed intangible and deferred tax assets, and (iii) other deductions from assets for leverage capital purposes.

Risk Management

Overview

Like all financial services companies, we engage in business activities and assume the related risks. The most significant risks we face are credit, compliance, operational, liquidity, market, reputation, strategic, and model risks. Our risk management activities are focused on ensuring that we properly identify, measure, and manage such risks across the entire enterprise to maintain safety and soundness, and to maximize profitability.

The Board serves in an oversight capacity, ensuring that Key's risks are managed in a manner that is not only effective and balanced, but also adds value for the shareholders. The Board understands Key's risk philosophy, approves the risk appetite, inquires about risk practices, reviews the portfolio of risks, compares the actual risks to the risk appetite, and is apprised of significant risks, both actual and emerging, and determines whether management is responding appropriately. The Board challenges management and ensures accountability.

The Board's Audit Committee assists the Board in oversight of financial statement integrity, regulatory and legal requirements, independent auditors' qualifications and independence, and the performance of the internal audit function and independent auditors. The Audit Committee meets with management and approves significant policies relating to the risk areas overseen by the Audit Committee. The Audit Committee has responsibility over all risk

Table of Contents

review functions, including internal audit, as well as financial reporting, legal matters, and fraud risk. The Audit Committee also receives reports on enterprise risk. In addition to regularly scheduled bi-monthly meetings, the Audit Committee convenes to discuss the content of our financial disclosures and quarterly earnings releases.

The Board's Risk Committee assists the Board in oversight of strategies, policies, procedures, and practices relating to the assessment and management of enterprise-wide risk, including credit, market, liquidity, model, operational, compliance, reputation, and strategic risks. The Risk Committee also assists the Board in overseeing risks related to capital adequacy, capital planning, and capital actions. The Risk Committee reviews and provides oversight of management's activities related to the enterprise-wide risk management framework, which includes review of the ERM Policy, including the Risk Appetite Statement, and management and ERM reports. The Risk Committee also approves any material changes to the charter of the ERM Committee and significant policies relating to risk management.

The Audit and Risk Committees meet jointly, as appropriate, to discuss matters that relate to each committee's responsibilities. Committee chairpersons routinely meet with management during interim months to plan agendas for upcoming meetings and to discuss emerging trends and events that have transpired since the preceding meeting. All members of the Board receive formal reports designed to keep them abreast of significant developments during the interim months.

Our ERM Committee, chaired by the Chief Executive Officer and comprising other senior level executives, is responsible for managing risk and ensuring that the corporate risk profile is managed in a manner consistent with our risk appetite. The ERM Program encompasses our risk philosophy, policy, framework, and governance structure for the management of risks across the entire company. The ERM Committee reports to the Board's Risk Committee. Annually, the Board reviews and approves the ERM Policy, as well as the risk appetite, including corporate risk tolerances for major risk categories. We use a risk-adjusted capital framework to manage risks. This framework is approved and managed by the ERM Committee.

Tier 2 Risk Governance Committees support the ERM Committee by identifying early warning events and trends, escalating emerging risks, and discussing forward-looking assessments. Risk Governance Committees include attendees from each of the Three Lines of Defense. The First Line of Defense is the line of business primarily responsible to accept, own, proactively identify, monitor, and manage risk. The Second Line of Defense comprises Risk Management representatives who provide independent, centralized oversight over all risk categories by aggregating, analyzing, and reporting risk information. Risk Review, our internal audit function, provides the Third Line of Defense in its role to provide independent assessment and testing of the effectiveness of, appropriateness of, and adherence to KeyCorp's risk management policies, practices, and controls. The Chief Risk Officer ensures that relevant risk information is properly integrated into strategic and business decisions, ensures appropriate ownership of risks, provides input into performance and compensation decisions, assesses aggregate enterprise risk, monitors capabilities to manage critical risks, and executes appropriate Board and stakeholder reporting.

Federal banking regulators continue to emphasize with financial institutions the importance of relating capital management strategy to the level of risk at each institution. We believe our internal risk management processes help us achieve and maintain capital levels that are commensurate with our business activities and risks, and conform to regulatory expectations.

Market risk management

Market risk is the risk that movements in market risk factors, including interest rates, foreign exchange rates, equity prices, commodity prices, credit spreads, and volatilities will reduce Key's income and the value of its portfolios. These factors influence prospective yields, values, or prices associated with the instrument.

We are exposed to market risk both in our trading and nontrading activities, which include asset and liability management activities. Our trading positions are carried at fair value with changes recorded in the income statement. These positions are subject to various market-based risk factors that affect the fair value of the financial instruments in the trading category. Information regarding our fair value policies, procedures, and methodologies is provided in Note 1 (“Summary of Significant Accounting Policies”) under the heading “Fair Value Measurements” on page 110 of our 2016 Form 10-K and Note 6 (“Fair Value Measurements”) in this report. Our traditional banking loan and deposit products, as well as long-term debt and certain short-term borrowings are nontrading positions. These positions are generally carried at the principal amount outstanding for assets and the amount

Table of Contents

owed for liabilities. The nontrading positions are subject to changes in economic value due to varying market conditions, primarily changes in interest rates.

Trading market risk

Key incurs market risk as a result of trading activities that are used in support of client facilitation and hedging activities, principally within our investment banking and capital markets businesses. Key has exposures to a wide range of interest rates, equity prices, foreign exchange rates, credit spreads, and commodity prices, as well as the associated implied volatilities and spreads. Our primary market risk exposures are a result of trading activities in the derivative and fixed income markets, and of maintaining positions in these instruments. We maintain modest trading inventories to facilitate customer flow, make markets in securities, and hedge certain risks. The majority of our positions are traded in active markets.

Management of trading market risks. Market risk management is an integral part of Key's risk culture. The Risk Committee of our Board provides oversight of trading market risks. The ERM Committee and the Market Risk Committee regularly review and discuss market risk reports prepared by our MRM that contain our market risk exposures and results of monitoring activities. Market risk policies and procedures have been defined and approved by the Market Risk Committee, a Tier 2 Risk Governance Committee, and take into account our tolerance for risk and consideration for the business environment.

The MRM, as the second line of defense, is an independent risk management function that partners with the lines of business to identify, measure, and monitor market risks throughout our company. The MRM is responsible for ensuring transparency of significant market risks, monitoring compliance with established limits, and escalating limit exceptions to appropriate senior management. The various business units and trading desks are responsible for ensuring that market risk exposures are well-managed and prudent. Market risk is monitored through various measures, such as VaR, and through routine stress testing, sensitivity, and scenario analyses. The MRM conducts stress tests for each position using historical worst case and standard shock scenarios. VaR, stressed VaR, and other analyses are prepared daily and distributed to appropriate management.

Covered positions. We monitor the market risk of our covered positions as defined in the Market Risk Rule, which includes all of our trading positions as well as all foreign exchange and commodity positions, regardless of whether the position is in a trading account. Instruments that are used to hedge nontrading activities, such as bank-issued debt and loan portfolios, equity positions that are not actively traded, and securities financing activities, do not meet the definition of a covered position. The MRM is responsible for identifying our portfolios as either covered or non-covered. The Covered Position Working Group develops the final list of covered positions, and a summary is provided to the Market Risk Committee.

Our significant portfolios of covered positions are detailed below. We analyze market risk by portfolios of covered positions, and do not separately measure and monitor our portfolios by risk type. The descriptions below incorporate the respective risk types associated with each of these portfolios.

- Fixed income includes those instruments associated with our capital markets business and the trading of securities as a dealer. These instruments may include positions in municipal bonds, bonds backed by the U.S. government, agency and corporate bonds, certain mortgage-backed securities, securities issued by the U.S. Treasury, money markets, and certain CMOs. The activities and instruments within the fixed income portfolio create exposures to interest rate and credit spread risks.

- Interest rate derivatives include interest rate swaps, caps, and floors, which are transacted primarily to accommodate the needs of commercial loan clients. In addition, we enter into interest rate derivatives to offset or mitigate the interest rate risk related to the client positions. The activities within this portfolio create exposures to interest rate risk.

VaR and stressed VaR. VaR is the estimate of the maximum amount of loss on an instrument or portfolio due to adverse market conditions during a given time interval within a stated confidence level. Stressed VaR is used to assess extreme conditions on market risk within our trading portfolios. MRM calculates VaR and stressed VaR on a daily basis, and the results are distributed to appropriate management. VaR and stressed VaR results are also provided to our regulators and utilized in regulatory capital calculations.

Table of Contents

We use a historical simulation VaR model to measure the potential adverse effect of changes in interest rates, foreign exchange rates, equity prices, and credit spreads on the fair value of our covered positions and other non-covered positions. Historical scenarios are customized for specific positions, and numerous risk factors are incorporated in the calculation. Additional consideration is given to the risk factors to estimate the exposures that contain optionality features, such as options and cancelable provisions. VaR is calculated using daily observations over a one-year time horizon, and approximates a 95% confidence level. Statistically, this means that we would expect to incur losses greater than VaR, on average, five out of 100 trading days, or three to four times each quarter. We also calculate VaR and stressed VaR at a 99% confidence level.

The VaR model is an effective tool in estimating ranges of possible gains and losses on our positions. However, there are limitations inherent in the VaR model since it uses historical results over a given time interval to estimate future performance. Historical results may not be indicative of future results, and changes in the market or composition of our portfolios could have a significant impact on the accuracy of the VaR model. We regularly review and enhance the modeling techniques, inputs and assumptions used. Our market risk policy includes the independent validation of our VaR model by Key's internal model validation group on an annual basis. The Model Risk Management Committee oversees the Model Validation Program, and results of validations are discussed with the ERM Committee.

Actual losses for the total covered positions did not exceed aggregate daily VaR on any day during the quarters ended September 30, 2017, and September 30, 2016. The MRM backtests our VaR model on a daily basis to evaluate its predictive power. The test compares VaR model results at the 99% confidence level to daily held profit and loss. Results of backtesting are provided to the Market Risk Committee. Backtesting exceptions occur when trading losses exceed VaR. We do not engage in correlation trading, or utilize the internal model approach for measuring default and credit migration risk. Our net VaR approach incorporates diversification, but our VaR calculation does not include the impact of counterparty risk and our own credit spreads on derivatives.

The aggregate VaR at the 99% confidence level with a one day holding period for all covered positions was $.6 million at September 30, 2017, and $1.1 million at September 30, 2016. The decrease in aggregate VaR was primarily due to the decreased exposure in our fixed income portfolios. Starting with the 3Q17, the aggregate VaR does not include the VaR for the credit derivatives that represented the hedging activities for the commercial real estate warehouse portfolio. These activities are no longer considered as covered portfolio. Figure 27 summarizes our VaR at the 99% confidence level with one day holding period for significant portfolios of covered positions for the three months ended September 30, 2017, and September 30, 2016. During these periods, none of our significant portfolios daily trading VaR numbers exceeded their VaR limits.

Figure 27. VaR for Significant Portfolios of Covered Positions

	2017				2016			
	Three months ended September 30,				Three months ended September 30,			
in millions	High	Low	Mean	September 30,	High	Low	Mean	September 30,
Trading account assets:								
Fixed income	$ 1.0	$ .3	$ .6	$ .3	$ .7	$ .3	$ .4	$ .5
Derivatives:								
Interest rate	$ .2	$ .1	$ .1	$ .1	$ .2	$ —	$ .1	$ .1
Credit	—	—	—	—	.3	.1	.2	.3

Stressed VaR is calculated using our general VaR results at the 99% confidence level and applying certain assumptions. The aggregate stressed VaR for all covered positions was $2.9 million at September 30, 2017, and $2.9 million at September 30, 2016. Figure 28 summarizes our stressed VaR at the 99% confidence level with a one day holding period for significant portfolios of covered positions for the three months ended September 30, 2017, and September 30, 2016.

Table of Contents

Figure 28. Stressed VaR for Significant Portfolios of Covered Positions

in millions	2017 Three months ended September 30, High	Low	Mean	September 30,	2016 Three months ended September 30, High	Low	Mean	September 30,
Trading account assets:								
Fixed income	$4.0	$1.9	$ 2.5	$ 1.9	$1.8	$ .9	$ 1.3	$ 1.5
Derivatives:								
Interest rate	$ .4	$ .1	$ .2	$ .4	$ .3	$ .1	$ .1	$ .3
Credit	—	—	—	—	.8	.2	.5	.7

Internal capital adequacy assessment. Market risk is a component of our internal capital adequacy assessment. Our risk-weighted assets include a market risk-equivalent asset amount, which consists of a VaR component, stressed VaR component, a de minimis exposure amount, and a specific risk add-on including the securitization positions. The aggregate amount for the securitization positions as defined by the Market Risk Rule was $26.1 million at September 30, 2017. Specific risk is the price risk of individual financial instruments, which is not accounted for by changes in broad market risk factors and is measured through a standardized approach. Market risk weighted assets, including the specific risk calculations, are run quarterly by the MRM and approved by the Chief Market Risk Officer.

Nontrading market risk

Most of our nontrading market risk is derived from interest rate fluctuations and its impacts on our traditional loan and deposit products, as well as investments, hedging relationships, long-term debt, and certain short-term borrowings. Interest rate risk, which is inherent in the banking industry, is measured by the potential for fluctuations in net interest income and the EVE. Such fluctuations may result from changes in interest rates and differences in the repricing and maturity characteristics of interest-earning assets and interest-bearing liabilities. We manage the exposure to changes in net interest income and the EVE in accordance with our risk appetite and within Board-approved policy limits.

Interest rate risk positions are influenced by a number of factors including the balance sheet positioning that arises out of customer preferences for loan and deposit products, economic conditions, the competitive environment within our markets, changes in market interest rates that affect client activity, and our hedging, investing, funding, and capital positions. The primary components of interest rate risk exposure consist of reprice risk, basis risk, yield curve risk, and option risk.

- Reprice risk is the exposure to changes in the level of interest rates and occurs when the volume of interest-bearing liabilities and the volume of interest-earning assets they fund (e.g., deposits used to fund loans) do not mature or reprice at the same time.

- Basis risk is the exposure to asymmetrical changes in interest rate indices and occurs when floating-rate assets and floating-rate liabilities reprice at the same time, but in response to different market factors or indices.

- Yield curve risk is the exposure to nonparallel changes in the slope of the yield curve (where the yield curve depicts the relationship between the yield on a particular type of security and its term to maturity) and occurs when interest-bearing liabilities and the interest-earning assets that they fund do not price or reprice to the same term point on the yield curve.

- Option risk is the exposure to a customer or counterparty's ability to take advantage of the interest rate environment and terminate or reprice one of our assets, liabilities, or off-balance sheet instruments prior to contractual maturity without a penalty. Option risk occurs when exposures to customer and counterparty early withdrawals or prepayments are not mitigated with an offsetting position or appropriate compensation.

The management of nontrading market risk is centralized within Corporate Treasury. The Risk Committee of our Board provides oversight of nontrading market risk. The ERM Committee and the ALCO review reports on the components of interest rate risk described above as well as sensitivity analyses of these exposures. These committees have various responsibilities related to managing nontrading market risk, including recommending, approving, and monitoring strategies that maintain risk positions within approved tolerance ranges. The A/LM policy provides the framework for the oversight and management of interest rate risk and is administered by the ALCO.

Table of Contents

Internal and external emerging issues are monitored on a daily basis. The MRM, as the second line of defense, provides additional oversight.

Net interest income simulation analysis. The primary tool we use to measure our interest rate risk is simulation analysis. For purposes of this analysis, we estimate our net interest income based on the current and projected composition of our on- and off-balance sheet positions, accounting for recent and anticipated trends in customer activity. The analysis also incorporates assumptions for the current and projected interest rate environments, and balance sheet growth projections based on a most likely macroeconomic view. While simulation modeling assumes that residual risk exposures are managed within the risk appetite and Board approved policy limits, the results also reflect management's desired interest rate risk positioning. Achieving the current modeled position typically requires purchases of investment securities to replace security cash flows and the execution of new interest rate swaps to replace maturing interest rate swaps. The simulation model estimates the amount of net interest income at risk by simulating the change in net interest income that would occur if interest rates were to gradually increase or decrease over the next 12 months. Our standard rate scenarios encompass a gradual, parallel increase or decrease of 200 basis points, but due to the low interest rate environment, we have modified the standard decrease scenario to a gradual, parallel decrease of 125 basis points over eight months with no change over the following four months. After calculating the amount of net interest income at risk to interest rate changes, we compare that amount with the base case of an unchanged interest rate environment.

Figure 29 presents the results of the simulation analysis at September 30, 2017, and September 30, 2016. At September 30, 2017, our simulated impact to changes in interest rates was modestly asset-sensitive. In June 2017, the Federal Reserve increased the range for the Federal Funds Target Rate, which led to an increase in the magnitude of the declining rate scenario to 125 basis points. Tolerance levels for risk management require the development of remediation plans to maintain residual risk within tolerance if simulation modeling demonstrates that a gradual, parallel 200 basis point increase or 125 basis point decrease in interest rates over the next 12 months would adversely affect net interest income over the same period by more than 5.5%. As a result of the Federal Reserve's June 2017 interest rate increase, our modeled exposure to declining rates increased. As shown in Figure 29, we are operating within these levels as of September 30, 2017.

Figure 29. Simulated Change in Net Interest Income

September 30, 2017		
Basis point change assumption (short-term rates)	-125	+200
Tolerance level	-5.50%	-5.50%
Interest rate risk assessment	-5.24%	1.07 %
September 30, 2016		
Basis point change assumption (short-term rates)	-50	+200
Tolerance level	-4.00%	-4.00%
Interest rate risk assessment	-2.73%	1.96 %

Simulation analysis produces a sophisticated estimate of interest rate exposure based on judgments related to assumptions input into the model. We tailor certain assumptions to the specific interest rate environment and yield curve shape being modeled, and validate those assumptions on a regular basis. However, actual results may differ from those derived in simulation analysis due to unanticipated changes to the balance sheet composition, customer behavior, product pricing, market interest rates, changes in management's desired interest rate risk positioning, investment, funding and hedging activities, and repercussions from unanticipated or unknown events.

We also perform regular stress tests and sensitivity analyses on the model inputs that could materially change the resulting risk assessments. Assessments are performed using different shapes of the yield curve, including steepening or flattening of the yield curve, changes in credit spreads, immediate changes in market interest rates, and changes in the relationship of money market interest rates. Assessments are also performed on changes to the following assumptions: loan and deposit balances, the pricing of deposits without contractual maturities, changes in lending spreads, prepayments on loans and securities, investment, funding and hedging activities, and liquidity and capital management strategies.

The results of additional assessments indicate that net interest income could increase or decrease from the base simulation results presented in Figure 29. Net interest income is highly dependent on the timing, magnitude, frequency, and path of interest rate increases and the associated assumptions for deposit repricing relationships, lending spreads, and the balance behavior of transaction accounts. The modeling is sensitive to the volume of fixed-rate assets and liabilities incorporated. The modeling currently assumes approximately $25.5 billion of investment security purchases and swap executions over the next three years. For every immediate reduction in fixed-rate assets of $1 billion, the modeled benefit to rising rates would increase by approximately 30 basis points. The low level of interest rates increases the uncertainty of assumptions for deposit balance behavior and deposit repricing relationships to market interest rates. Our historical deposit repricing betas in the last rising rate cycle ranged between 50% and 60% for interest-bearing deposits, and we continue to make similar assumptions in our modeling, with the modeled betas varying by customer segment and product type. Recent deposit repricing has been lower than our modeled assumptions, and has contributed to the increase in the modeled exposure to declining interest rates since the Federal Reserve began raising rates in 2015. In the modeling, if the deposit beta for the first 25 basis point increase in the Federal Funds Target Rate was zero, then returned to the standard modeled betas for the next 175 basis points of rate increases, our modeled asset sensitive benefit would increase by approximately 225 basis points. The sensitivity testing of assumptions supports our confidence that actual results are likely to be within 100 basis points of modeled results.

Our current interest rate risk position could fluctuate to higher or lower levels of risk depending on the competitive environment and client behavior that may affect the actual volume, mix, maturity, and repricing characteristics of loan and deposit flows. Treasury discretionary activities related to funding, investing, and hedging may also change as a result of changes in customer business flows, or changes in management’s desired interest rate risk positioning. As changes occur to both the configuration of the balance sheet and the outlook for the economy, management proactively evaluates hedging opportunities that may change our interest rate risk profile.

We also conduct simulations that measure the effect of changes in market interest rates in the second and third years of a three-year horizon. These simulations are conducted in a manner similar to those based on a 12-month horizon. To capture longer-term exposures, we calculate exposures to changes of the EVE as discussed in the following section.

Economic value of equity modeling. EVE complements net interest income simulation analysis as it estimates risk exposure beyond 12-, 24-, and 36-month horizons. EVE modeling measures the extent to which the economic values of assets, liabilities and off-balance sheet instruments may change in response to fluctuations in interest rates. EVE is calculated by subjecting the balance sheet to an immediate 200 basis point increase or decrease in interest rates, measuring the resulting change in the values of assets, liabilities, and off-balance sheet instruments, and comparing those amounts with the base case of the current interest rate environment. Because the calculation of EVE under an immediate 200 basis point decrease in interest rates in the current low rate environment results in certain interest rates declining to zero and a less than 200 basis point decrease in certain yield curve term points, we have modified the standard declining rate scenario to an immediate 125 basis point decrease. This analysis is highly dependent upon assumptions applied to assets and liabilities with non-contractual maturities. Those assumptions are based on historical behaviors, as well as our expectations. We develop remediation plans that would maintain residual risk within tolerance if this analysis indicates that our EVE will decrease by more than 15% in response to an immediate increase or decrease in interest rates. We are operating within these guidelines as of September 30, 2017.

Management of interest rate exposure. We use the results of our various interest rate risk analyses to formulate A/LM strategies to achieve the desired risk profile while managing to our objectives for capital adequacy and liquidity risk exposures. Specifically, we manage interest rate risk positions by purchasing securities, issuing term debt with floating or fixed interest rates, and using derivatives — predominantly in the form of interest rate swaps, which modify the interest rate characteristics of certain assets and liabilities.

Figure 30 shows all swap positions that we hold for A/LM purposes. These positions are used to convert the contractual interest rate index of agreed-upon amounts of assets and liabilities (i.e., notional amounts) to another interest rate index. For example, fixed-rate debt is converted to a floating rate through a “receive fixed/pay variable” interest rate swap. The volume, maturity and mix of portfolio swaps change frequently as we adjust our broader A/LM objectives and the balance sheet positions to be hedged. For more information about how we use interest rate swaps to manage our risk profile, see Note 8 (“Derivatives and Hedging Activities”).

Table of Contents

Figure 30. Portfolio Swaps by Interest Rate Risk Management Strategy

	September 30, 2017					September 30, 2016	
			Weighted-Average				
dollars in millions	Notional Amount	Fair Value	Maturity (Years)	Receive Rate	Pay Rate	Notional Amount	Fair Value
Receive fixed/pay variable — conventional A/LM [a]	$15,400	$(70)	1.9	1.2 %	1.2 %	$14,250	$105
Receive fixed/pay variable — conventional debt	9,883	45	2.8	1.6	1.2	8,473	293
Pay fixed/receive variable — conventional debt	50	(6)	10.8	1.3	3.6	50	(11)
Total portfolio swaps	$25,333	$(31) [b], [c]	2.3	1.4 %	1.2 %	$22,773	$387 [b]

(a) Portfolio swaps designated as A/LM are used to manage interest rate risk tied to both assets and liabilities.
(b) Excludes accrued interest of $88 million and $49 million at September 30, 2017, and September 30, 2016, respectively.
(c) Excludes variation margin payments for CME-cleared trades of $46 million at September 30, 2017.

Liquidity risk management

Liquidity risk, which is inherent in the banking industry, is measured by our ability to accommodate liability maturities and deposit withdrawals, meet contractual obligations, and fund new business opportunities at a reasonable cost, in a timely manner, and without adverse consequences. Liquidity management involves maintaining sufficient and diverse sources of funding to accommodate planned, as well as unanticipated, changes in assets and liabilities under both normal and adverse conditions.

Factors affecting liquidity

Our liquidity could be adversely affected by both direct and indirect events. An example of a direct event would be a downgrade in our public credit ratings by a rating agency. Examples of indirect events (events unrelated to us) that could impair our access to liquidity would be an act of terrorism or war, natural disasters, political events, or the default or bankruptcy of a major corporation, mutual fund or hedge fund. Similarly, market speculation, or rumors about us or the banking industry in general, may adversely affect the cost and availability of normal funding sources.

Our credit ratings at September 30, 2017, are shown in Figure 31. We believe these credit ratings, under normal conditions in the capital markets, would enable KeyCorp or KeyBank to issue fixed income securities to investors. On October 11, 2017, DBRS, Inc. upgraded ratings for KeyCorp and KeyBank, including the KeyCorp Senior Long-Term Debt Rating to A (low) from BBB (high).

Figure 31. Credit Ratings

September 30, 2017	Short-Term Borrowings	Long-Term Deposits	Senior Long-Term Debt	Subordinated Long-Term Debt	Capital Securities	Preferred Stock
KEYCORP (THE PARENT COMPANY)						
Standard & Poor’s	A-2	N/A	BBB+	BBB	BB+	BB+
Moody’s	P-2	N/A	Baa1	Baa1	Baa2	Baa3
Fitch Ratings, Inc.	F1	N/A	A-	BBB+	BB+	BB
DBRS, Inc.	R-2(high)	N/A	BBB(high)	BBB	BBB	BB(high)
KEYBANK						

Standard & Poor’s	A-2	N/A	A-	BBB+	N/A	N/A
Moody’s	P-1	Aa3	A3	Baa1	N/A	N/A
Fitch Ratings, Inc.	F1	A	A-	BBB+	N/A	N/A
DBRS, Inc.	R-1(low)	A(low)	A(low)	BBB(high)	N/A	N/A

Sources of liquidity

Our primary source of funding for the Bank is retail and commercial deposits. As of September 30, 2017, our loan-to-deposit ratio was 86%. In addition, we also have available unused sources of wholesale funding and liquid assets and borrowing capacity at the FHLB of Cincinnati and Federal Reserve Bank of Cleveland. Our liquid asset portfolio at September 30, 2017, totaled $25.4 billion, consisting of $21.4 billion of unpledged securities, $322 million of securities available for secured funding at the FHLB, and $3.7 billion of net balances of federal funds sold and balances in our Federal Reserve account. Additionally, as of September 30, 2017, our unused borrowing capacity secured by loan collateral was $22.9 billion at the Federal Reserve Bank of Cleveland and $4.9 billion at the FHLB. During the third quarter of 2017, our outstanding FHLB of Cincinnati advances were increased by $1.1 billion as term advances were added.

Table of Contents

During the third quarter of 2017, KeyBank issued $750 million of 2.30% Senior Bank Notes due September 14, 2022, under its Global Bank Note Program.

Liquidity for KeyCorp

The primary source of liquidity for KeyCorp is from subsidiary dividends, primarily from KeyBank. KeyCorp has sufficient liquidity when it can service its debt, support customary corporate operations and activities (including acquisitions), support occasional guarantees of subsidiaries' obligations in transactions with third parties at a reasonable cost, in a timely manner, and without adverse consequences, and pay dividends to shareholders.

At September 30, 2017, KeyCorp held $2.0 billion in cash, which we projected to be sufficient to meet our projected obligations, including the repayment of our maturing debt obligations for the periods prescribed by our risk tolerance.

Typically, KeyCorp meets its liquidity requirements through regular dividends from KeyBank. During the third quarter of 2017, KeyBank paid $250 million in dividends to KeyCorp. As of September 30, 2017, KeyBank had regulatory capacity to pay $877 million in dividends to KeyCorp without prior regulatory approval.

Our liquidity position and recent activity

Over the past quarter, our liquid asset portfolio, which includes overnight and short-term investments, as well as unencumbered, high quality liquid securities held as protection against a range of potential liquidity stress scenarios, has increased as a result of higher balances held at the Federal Reserve and an increase in unpledged securities. The liquid asset portfolio continues to exceed the amount that we estimate would be necessary to manage through an adverse liquidity event by providing sufficient time to develop and execute a longer-term solution.

We generate cash flows from operations and from investing and financing activities. We have approximately $179 million of cash, cash equivalents, and short-term investments in international tax jurisdictions as of September 30, 2017. As we consider alternative long-term strategic and liquidity plans, opportunities to repatriate these amounts would result in approximately $2 million in taxes to be paid. We have included the appropriate amount as a deferred tax liability at September 30, 2017.

The Consolidated Statements of Cash Flows summarize our sources and uses of cash by type of activity for the nine-month periods ended September 30, 2017, and September 30, 2016.

For more information regarding liquidity governance structure, factorings affecting liquidity, management of liquidity risk at KeyBank and KeyCorp, long-term liquidity strategies, and other liquidity programs see Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" on page 76 of our 2016 Form 10-K.

Credit risk management

Credit risk is the risk of loss arising from an obligor's inability or failure to meet contractual payment or performance terms. Like other financial services institutions, we make loans, extend credit, purchase securities, and enter into financial derivative contracts, all of which have related credit risk.

Credit policy, approval, and evaluation

We manage credit risk exposure through a multifaceted program. The Credit Risk Committee and the Commercial Credit Policy Committee approve retail and commercial credit policies. Significant policies are reviewed periodically with our Executive Risk Management Committee and the Risk Committee of our Board of Directors on a prescribed schedule. These policies are communicated throughout the organization to foster a consistent approach to granting credit.

Our credit risk management team and individuals within our lines of business to whom credit risk management has delegated authority are responsible for credit approval. Individuals with assigned credit authority are authorized to grant exceptions to credit policies. It is not unusual to make exceptions to established policies when mitigating circumstances dictate, however, a corporate tolerance has been established to keep exceptions at an acceptable level based upon portfolio and economic considerations.

Our credit risk management team uses risk models to evaluate consumer loans. These models, known as scorecards, forecast the probability of serious delinquency and default for an applicant. The scorecards are embedded in the application processing system, which allows for real-time scoring and automated decisions for many of our products. We periodically validate the loan grading and scoring processes. For more information see Note 5 (“Asset Quality“).

We maintain an active concentration management program to monitor concentration risk in our credit portfolios. For aggregate credit relationships, we employ a sliding scale of exposure, known as hold limits, which is dictated by the type of loan and strength of the borrower. Our legal lending limit is approximately $2.1 billion. However, internal hold limits generally restrict the largest exposures to less than 20% of that amount. As of September 30, 2017, we had ten client relationships with loan commitments net of credit default swaps of more than $200 million. The average amount outstanding on these ten individual net obligor commitments was $103 million at September 30, 2017. In general, our philosophy is to maintain a diverse portfolio with regard to credit exposures.

We actively manage the overall loan portfolio in a manner consistent with asset quality objectives and concentration risk tolerances to mitigate excess portfolio credit risk. We utilize credit default swaps on a limited basis to transfer a portion of the credit risk associated with a particular extension of credit to a third party. At September 30, 2017, we used credit default swaps with a notional amount of $184 million to manage the credit risk associated with specific commercial lending obligations. We may also sell credit derivatives — primarily single name credit default swaps — to offset our purchased credit default swap position prior to maturity. At September 30, 2017, we did not have any sold credit default swaps outstanding.

Credit default swaps are recorded on the balance sheet at fair value. Related gains or losses, as well as the premium paid or received for credit protection, are included in the “corporate services income” and “other income” components of noninterest income.

Allowance for loan and lease losses

At September 30, 2017, the ALLL was $880 million, or 1.02% of period-end loans, compared to $858 million, or 1.00%, at December 31, 2016. The allowance includes $22 million that was specifically allocated for impaired loans of $376 million at September 30, 2017, compared to $37 million that was specifically allocated for impaired loans of $501 million at December 31, 2016. For more information about impaired loans, see Note 5 (“Asset Quality”). At September 30, 2017, the ALLL was 170.2% of nonperforming loans, compared to 137.3% at December 31, 2016.

Selected asset quality statistics for each of the past five quarters are presented in Figure 32. The factors that drive these statistics are discussed in the remainder of this section.

Figure 32. Selected Asset Quality Statistics from Continuing Operations

	2017			2016	
dollars in millions	Third	Second	First	Fourth	Third
Net loan charge-offs	$32	$ 66	$58	$72	$44
Net loan charge-offs to average total loans	.15 %	.31 %	.27 %	.34 %	.23 %
Allowance for loan and lease losses	$880	$ 870	$870	$858	$865
Allowance for credit losses [(a)]	937	918	918	913	918
Allowance for loan and lease losses to period-end loans	1.02 %	1.01 %	1.01 %	1.00 %	1.01 %
Allowance for credit losses to period-end loans	1.08	1.06	1.07	1.06	1.07

Allowance for loan and lease losses to nonperforming loans [b]	170.2	171.6	151.8	137.3	119.6
Allowance for credit losses to nonperforming loans [b]	181.2	181.1	160.2	146.1	127.0
Nonperforming loans at period end [b]	$517	$ 507	$573	$625	$723
Nonperforming assets at period end [b]	556	556	623	676	760
Nonperforming loans to period-end portfolio loans [b]	.60 %	.59 %	.67 %	.73 %	.85 %
Nonperforming assets to period-end portfolio loans plus OREO and other nonperforming assets [b]	.64	.64	.72	.79	.89

(a) Includes the ALLL plus the liability for credit losses on lending-related unfunded commitments.

(b) Nonperforming loan balances exclude $783 million, $835 million, $812 million, $865 million, and $959 million of PCI loans at September 30, 2017, June 30, 2017, March 31, 2017, December 31, 2016, and September 30, 2016, respectively. The June 30, 2017 PCI loan balances increased from the March 31, 2017 balances, as a result of the finalization of the First Niagara Acquisition Date loan valuation, which increased the Acquisition Date of First Niagara PCI loans fair value by $105 million from the provisional estimate recorded in the 2016 10-K.

49

Table of Contents

We estimate the appropriate level of the ALLL on at least a quarterly basis. The methodology used is described in Note 1 ("Summary of Significant Accounting Policies") under the heading "Allowance for Loan and Lease Losses" beginning on page 109 of our 2016 Form 10-K. Briefly, our allowance applies expected loss rates to existing loans with similar risk characteristics. We exercise judgment to assess any adjustment to the expected loss rates for the impact of factors such as changes in economic conditions, lending policies including underwriting standards, and the level of credit risk associated with specific industries and markets. The ALLL at September 30, 2017, represents our best estimate of the probable credit losses inherent in the loan portfolio at that date.

As shown in Figure 33, our ALLL from continuing operations increased by $22 million, or 2.6%, from December 31, 2016. Our commercial ALLL increased by $26 million, or 3.6%, from December 31, 2016, primarily because of loan growth in certain segments of the commercial loan portfolio, as well as credit quality migration. Our consumer ALLL decreased by $4 million, or 2.8%, from December 31, 2016, primarily due to continued improvement in credit quality metrics, including improved delinquency trends, which have decreased expected loss rates. Also contributing to the increase was the ALLL on our acquired portfolio, which increased $36 million from December 31, 2016. The ALLL on the acquired portfolio was $72 million at September 30, 2017, representing .40% of our period-end acquired loans, compared to .17% at December 31, 2016.

Our liability for credit losses on lending-related commitments increased by $2 million from December 31, 2016, to $57 million at September 30, 2017. When combined with our ALLL, our total allowance for credit losses represented 1.08% of period-end loans at September 30, 2017, and 1.06% at December 31, 2016.

Figure 33. Allocation of the Allowance for Loan Lease Losses

dollars in millions	September 30, 2017 Amount	Percent of Allowance to Total Allowance	Percent of Loan Type to Total Loans	December 31, 2016 Amount	Percent of Allowance to Total Allowance	Percent of Loan Type to Total Loans
Commercial and industrial	$532	60.4 %	47.6 %	$508	59.2 %	46.2 %
Commercial real estate:						
Commercial mortgage	138	15.7	17.2	144	16.8	17.6
Construction	29	3.3	2.2	22	2.6	2.7
Total commercial real estate loans	167	19.0	19.4	166	19.4	20.3
Commercial lease financing	43	4.9	5.5	42	4.9	5.4
Total commercial loans	742	84.3	72.5	716	83.5	71.9
Real estate — residential mortgage	8	.9	6.3	17	2.0	6.5
Home equity loans	39	4.4	14.2	54	6.3	14.7
Consumer direct loans	28	3.2	2.1	24	2.8	2.1
Credit cards	44	5.0	1.2	38	4.4	1.3
Consumer indirect loans	19	2.2	3.7	9	1.0	3.5
Total consumer loans	138	15.7	27.5	142	16.5	28.1
Total loans [(a)]	$880	100.0 %	100.0 %	$858	100.0 %	100.0 %

(a) Excludes allocations of the ALLL related to the discontinued operations of the education lending business in the amount of $18 million, and $24 million at September 30, 2017, and December 31, 2016, respectively.

Our provision for credit losses was $51 million for the third quarter of 2017, compared to $59 million for the third quarter of 2016. Compared to the first nine months of 2016, oil and gas prices have stabilized, leading to improved credit quality metrics. We continue to reduce our exposure in our higher-risk businesses, including the residential properties portion of our construction loan portfolio, marine/RV financing, and other selected leasing portfolios through the sale of certain loans, payments from borrowers, or net loan charge-offs. The decrease in the third quarter of 2017 provision also reflects a large recovery in the commercial and industrial portfolio.

Net loan charge-offs

Net loan charge-offs for the third quarter of 2017 totaled $32 million, or .15% of average loans, compared to net loan charge-offs of $44 million, or .23%, for the same period last year. Figure 34 shows the trend in our net loan charge-offs by loan type, while the composition of loan charge-offs and recoveries by type of loan is presented in Figure 35.

Over the past 12 months, net loan charge-offs decreased $12 million. This decrease is attributable to continued portfolio strength and a large recovery in the commercial and industrial portfolio.

Table of Contents

Figure 34. Net Loan Charge-offs from Continuing Operations [(a)]

	2017			2016	
dollars in millions	Third	Second	First	Fourth	Third
Commercial and industrial	$4	$ 38	$ 27	$37	$ 15
Real estate — Commercial mortgage	5	3	—	2	(1)
Real estate — Construction	2	—	(1)	—	8
Commercial lease financing	(2)	1	5	—	5
Total commercial loans	9	42	31	39	27
Real estate — Residential mortgage	(1)	3	(4)	2	—
Home equity loans	2	4	5	4	2
Consumer direct loans	7	6	9	8	5
Credit cards	10	10	10	9	8
Consumer indirect loans	5	1	7	10	2
Total consumer loans	23	24	27	33	17
Total net loan charge-offs	$32	$ 66	$ 58	$72	$ 44
Net loan charge-offs to average loans	.15 %	.31 %	.27 %	.34 %	.23 %
Net loan charge-offs from discontinued operations — education lending business	$8	$ 2	$ 4	$4	$ 3

(a) Credit amounts indicate that recoveries exceeded charge-offs.

Table of Contents

Figure 35. Summary of Loan and Lease Loss Experience from Continuing Operations

	Three months ended September 30,		Nine months ended September 30,	
dollars in millions	2017	2016	2017	2016
Average loans outstanding	$86,814	$77,697	$86,485	$66,375
Allowance for loan and lease losses at beginning of period	$870	$854	$858	$796
Loans charged off:				
Commercial and industrial	29	17	101	78
Real estate — commercial mortgage	6	—	9	3
Real estate — construction	2	9	2	9
Total commercial real estate loans [a]	8	9	11	12
Commercial lease financing	1	5	9	11
Total commercial loans [b]	38	31	121	101
Real estate — residential mortgage	—	1	2	4
Home equity loans	6	5	23	22
Consumer direct loans	8	6	26	18
Credit cards	11	9	34	25
Consumer indirect loans	8	3	24	9
Total consumer loans	33	24	109	78
Total loans charged off	71	55	230	179
Recoveries:				
Commercial and industrial	25	2	32	8
Real estate — commercial mortgage	1	1	1	9
Real estate — construction	—	1	1	2
Total commercial real estate loans [a]	1	2	2	11
Commercial lease financing	3	—	5	2
Total commercial loans [b]	29	4	39	21
Real estate — residential mortgage	1	1	4	3
Home equity loans	4	3	12	10
Consumer direct loans	1	1	4	4
Credit cards	1	1	4	3
Consumer indirect loans	3	1	11	5
Total consumer loans	10	7	35	25
Total recoveries	39	11	74	46
Net loan charge-offs	(32)	(44)	(156)	(133)
Provision (credit) for loan and lease losses	42	56	178	203
Foreign currency translation adjustment	—	(1)	—	(1)
Allowance for loan and lease losses at end of period	$880	$865	$880	$865
Liability for credit losses on lending-related commitments at beginning of period	$48	$50	$55	$56
Provision (credit) for losses on lending-related commitments	9	3	2	(3)
Liability for credit losses on lending-related commitments at end of period [c]	$57	$53	$57	$53
Total allowance for credit losses at end of period	$937	$918	$937	$918
Net loan charge-offs to average total loans	.15 %	.23 %	.24 %	.27 %
Allowance for loan and lease losses to period-end loans	1.02	1.01 %	1.02	1.01
Allowance for credit losses to period-end loans	1.08	1.07 %	1.08	1.07

Allowance for loan and lease losses to nonperforming loans	170.2	119.6 %	170.2	119.6
Allowance for credit losses to nonperforming loans	181.2	127.0 %	181.2	127.0
Discontinued operations — education lending business:				
Loans charged off	$10	$6	$20	$21
Recoveries	2	3	6	8
Net loan charge-offs	$(8)	$(3)	$(14)	$(13)

(a) See Figure 18 entitled "Commercial Real Estate Loans" and the accompanying discussion in the "Loans and loans held for sale" section for more information related to our commercial real estate loan portfolio.

(b) See Figure 17 entitled "Commercial Loans by Industry" and the accompanying discussion in the "Loans and loans held for sale" section for more information related to our commercial loan portfolio.

(c) Included in "accrued expense and other liabilities" on the balance sheet.

Table of Contents

Nonperforming assets

Figure 36 shows the composition of our nonperforming assets. These assets totaled $556 million at September 30, 2017, and represented .64% of period-end portfolio loans, OREO, and other nonperforming assets, compared to $676 million, or .79%, at December 31, 2016. See Note 1 ("Summary of Significant Accounting Policies") under the headings "Nonperforming Loans," "Impaired Loans," and "Allowance for Loan and Lease Losses" beginning on page 108 of our 2016 Form 10-K for a summary of our nonaccrual and charge-off policies.

Figure 36. Summary of Nonperforming Assets and Past Due Loans from Continuing Operations

dollars in millions	September 30, 2017	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016
Commercial and industrial	$ 169	$ 178	$ 258	$ 297	$ 335
Real estate — commercial mortgage	30	34	32	26	32
Real estate — construction	2	4	2	3	17
Total commercial real estate loans [(a)]	32	38	34	29	49
Commercial lease financing	11	11	5	8	13
Total commercial loans [(b)]	212	227	297	334	397
Real estate — residential mortgage	57	58	54	56	72
Home equity loans	227	208	207	223	225
Consumer direct loans	3	2	3	6	2
Credit cards	2	2	3	2	3
Consumer indirect loans	16	10	9	4	24
Total consumer loans	305	280	276	291	326
Total nonperforming loans [(c)]	517	507	573	625	723
OREO	39	48	49	51	35
Other nonperforming assets	—	1	1	—	2
Total nonperforming assets [(c)]	$ 556	$ 556	$ 623	$ 676	$ 760
Accruing loans past due 90 days or more	$ 86	$ 85	$ 79	$ 87	$ 49
Accruing loans past due 30 through 89 days	329	340	312	404	317
Restructured loans — accruing and nonaccruing [(d)]	315	333	302	280	304
Restructured loans included in nonperforming loans [(d)]	187	193	161	141	149
Nonperforming assets from discontinued operations — education lending business	8	5	4	5	5
Nonperforming loans to period-end portfolio loans [(c)]	.60 %	.59 %	.67 %	.73 %	.85 %
Nonperforming assets to period-end portfolio loans plus OREO and other nonperforming assets [(c)]	.64 %	.64 %	.72 %	.79 %	.89 %

(a) See Figure 18 and the accompanying discussion in the "Loans and loans held for sale" section for more information related to our commercial real estate loan portfolio.

(b) See Figure 17 and the accompanying discussion in the "Loans and loans held for sale" section for more information related to our commercial loan portfolio.

(c) Nonperforming loan balances exclude $783 million, $835 million, $812 million, $865 million, and $959 million of PCI loans at September 30, 2017, June 30, 2017, March 31, 2017, December 31, 2016, and September 30, 2016, respectively.

(d) Restructured loans (i.e., TDRs) are those for which Key, for reasons related to a borrower's financial difficulties, grants a concession to the borrower that it would not otherwise consider. These concessions are made to improve the collectability of the loan and generally take the form of a reduction of the interest rate, extension of the maturity date or reduction in the principal balance.

As shown in Figure 36, nonperforming assets at September 30, 2017, decreased $120 million from December 31, 2016. This decrease was a result of an increase in nonperforming loans being returned to accrual and an increase in payments received on nonperforming loans.

Table of Contents

Figure 37 shows the types of activity that caused the change in our nonperforming loan balance during each of the last five quarters.

Figure 37. Summary of Changes in Nonperforming Loans from Continuing Operations

	2017			2016	
in millions	Third	Second	First	Fourth	Third
Balance at beginning of period	$507	$573	$625	$723	$619
Loans placed on nonaccrual status	181	143	218	170	78
Nonperforming loans acquired from First Niagara	—	—	—	(31)	150
Charge-offs	(71)	(82)	(77)	(81)	(53)
Loans sold	(1)	—	(8)	(9)	—
Payments	(32)	(84)	(59)	(30)	(32)
Transfers to OREO	(10)	(8)	(11)	(21)	(5)
Transfers to other nonperforming assets	—	—	—	—	—
Loans returned to accrual status	(57)	(35)	(115)	(96)	(34)
Balance at end of period [(a)]	$517	$507	$573	$625	$723

(a) Nonperforming loan balances exclude $783 million, $835 million, $812 million, $865 million, and $959 million of PCI loans at September 30, 2017, June 30, 2017, March 31, 2017, December 31, 2016, and September 30, 2016, respectively.

Operational and compliance risk management

Like all businesses, we are subject to operational risk, which is the risk of loss resulting from human error or malfeasance, inadequate or failed internal processes and systems, and external events. These events include, among other things, threats to our cybersecurity, as we are reliant upon information systems and the Internet to conduct our business activities. Operational risk also encompasses compliance risk, which is the risk of loss from violations of, or noncompliance with, laws, rules and regulations, prescribed practices, and ethical standards. Under the Dodd-Frank Act, large financial companies like Key are subject to heightened prudential standards and regulation. This heightened level of regulation has increased our operational risk. Resulting operational risk losses and/or additional regulatory compliance costs could take the form of explicit charges, increased operational costs, harm to our reputation, or foregone opportunities.

We seek to mitigate operational risk through identification and measurement of risk, alignment of business strategies with risk appetite and tolerance, and a system of internal controls and reporting. We continuously strive to strengthen our system of internal controls to improve the oversight of our operational risk and to ensure compliance with laws, rules, and regulations. For example, an operational event database tracks the amounts and sources of operational risk and losses. This tracking mechanism helps to identify weaknesses and to highlight the need to take corrective action. We also rely upon software programs designed to assist in assessing operational risk and monitoring our control processes. This technology has enhanced the reporting of the effectiveness of our controls to senior management and the Board.

The Operational Risk Management Program provides the framework for the structure, governance, roles, and responsibilities, as well as the content, to manage operational risk for Key. The Compliance Risk Committee serves the same function in managing compliance risk for Key. Primary responsibility for managing and monitoring internal control mechanisms lies with the managers of our various lines of business. The Operational Risk Committee and Compliance Risk Committee are senior management committees that oversee our level of operational and compliance risk and direct and support our operational and compliance infrastructure and related activities. These committees and the Operational Risk Management and Compliance functions are an integral part of our ERM Program. Our Risk Review function regularly assesses the overall effectiveness of our Operational Risk Management and Compliance

Programs and our system of internal controls. Risk Review reports the results of reviews on internal controls and systems to senior management and the Risk and Audit Committees and independently supports the Risk Committee's oversight of these controls.

Cybersecurity

We maintain comprehensive Cyber Incident Response Plans, and we devote significant time and resources to maintaining and regularly updating our technology systems and processes to protect the security of our computer systems, software, networks, and other technology assets against attempts by third parties to obtain unauthorized access to confidential information, destroy data, disrupt or degrade service, sabotage systems, or cause other damage. We and many other U.S. financial institutions have experienced distributed denial-of-service attacks from technologically sophisticated third parties. These attacks are intended to disrupt or disable online banking services and prevent banking transactions. We also periodically experience other attempts to breach the security of our

Table of Contents

systems and data. These cyberattacks have not, to date, resulted in any material disruption of our operations or material harm to our customers, and have not had a material adverse effect on our results of operations.

Cyberattack risks may also occur with our third-party technology service providers, and may result in financial loss or liability that could adversely affect our financial condition or results of operations. Cyberattacks could also interfere with third-party providers' ability to fulfill their contractual obligations to us. Recent high-profile cyberattacks have targeted retailers, credit bureaus, and other businesses for the purpose of acquiring the confidential information (including personal, financial, and credit card information) of customers, some of whom are customers of ours. We may incur expenses related to the investigation of such attacks or related to the protection of our customers from identity theft as a result of such attacks. We may also incur expenses to enhance our systems or processes in order to protect our customers whose information may have been exposed through the recent breach of the Equifax credit bureau or other external security incidents. Risks and exposures related to cyberattacks are expected to remain high for the foreseeable future due to the rapidly evolving nature and sophistication of these threats, as well as due to the expanding use of Internet banking, mobile banking, and other technology-based products and services by us and our clients.

Critical Accounting Policies and Estimates

Our business is dynamic and complex. Consequently, we must exercise judgment in choosing and applying accounting policies and methodologies. These choices are critical – not only are they necessary to comply with GAAP, they also reflect our view of the appropriate way to record and report our overall financial performance. All accounting policies are important, and all policies described in Note 1 ("Summary of Significant Accounting Policies") beginning on page 106 of our 2016 Form 10-K should be reviewed for a greater understanding of how we record and report our financial performance.

In our opinion, some accounting policies are more likely than others to have a critical effect on our financial results and to expose those results to potentially greater volatility. These policies apply to areas of relatively greater business importance, or require us to exercise judgment and to make assumptions and estimates that affect amounts reported in the financial statements. Because these assumptions and estimates are based on current circumstances, they may prove to be inaccurate, or we may find it necessary to change them.

We rely heavily on the use of judgment, assumptions, and estimates to make a number of core decisions, including accounting for the ALLL; contingent liabilities, guarantees and income taxes; derivatives and related hedging activities; and assets and liabilities that involve valuation methodologies. In addition, we may employ outside valuation experts to assist us in determining fair values of certain assets and liabilities. A brief discussion of each of these areas appears on pages 92 through 95 of our 2016 Form 10-K.

At September 30, 2017, $20.6 billion, or 15%, of our total assets were measured at fair value on a recurring basis. Approximately 99% of these assets, before netting adjustments, were classified as Level 1 or Level 2 within the fair value hierarchy. At September 30, 2017, $848 million, or 1%, of our total liabilities were measured at fair value on a recurring basis. Approximately 99% of these liabilities were classified as Level 1 or Level 2.

At September 30, 2017, $18 million, or less than 1% of our total assets were measured at fair value on a nonrecurring basis. All of these assets were classified as Level 3. At September 30, 2017, there were no liabilities measured at fair value on a nonrecurring basis.

During the first nine months of 2017, we did not significantly alter the manner in which we applied our critical accounting policies or developed related assumptions and estimates.

Table of Contents

European Sovereign and Nonsovereign Debt Exposures

Our total European sovereign and Nonsovereign debt exposure is presented in Figure 38.

Figure 38. European Sovereign and Nonsovereign Debt Exposures

September 30, 2017 in millions	Short-and Long-Term Commercial Total [(a)]	Foreign Exchange and Derivatives with Collateral [(b)]	Net Exposure
France:			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	$ 4	$ 4
Nonsovereign non-financial institutions	$ 10	—	10
Total	10	4	14
Germany:			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	—	—
Nonsovereign non-financial institutions	33	—	33
Total	33	—	33
Italy:			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	—	—
Nonsovereign non-financial institutions	10	—	10
Total	10	—	10
Netherlands:			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	—	—
Nonsovereign non-financial institutions	4	—	4
Total	4	—	4
Spain:			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	—	—
Nonsovereign non-financial institutions	3	—	3
Total	3	—	3
Switzerland:			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	(2)	(2)
Nonsovereign non-financial institutions	51	—	51
Total	51	(2)	49
United Kingdom:			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	185	185
Nonsovereign non-financial institutions	35	—	35
Total	35	185	220
Other Europe: [(c)]			
Sovereigns	—	—	—
Nonsovereign financial institutions	—	—	—
Nonsovereign non-financial institutions	1	—	1
Total	1	—	1
Total Europe:			

Sovereigns	—	—	—
Nonsovereign financial institutions	—	187	187
Nonsovereign non-financial institutions	147	—	147
Total	$ 147	$ 187	$ 334

(a) Represents our outstanding leases.

(b) Represents contracts to hedge our balance sheet asset and liability needs, and to accommodate our clients' trading and/or hedging needs. Our derivative mark-to-market exposures are calculated and reported on a daily basis. These exposures are largely covered by cash or highly marketable securities collateral with daily collateral calls.

(c) Other Europe consists of the following countries: Austria, Belarus, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Finland, Greece, Hungary, Iceland, Ireland, Lithuania, Luxembourg, Malta, Norway, Poland, Portugal, Romania, Russia, Slovakia, Slovenia, Sweden, and Ukraine. 100% of our current exposure in Other Europe is in Austria, Belgium, Romania, and Sweden.

Our credit risk exposure is largely concentrated in developed countries with emerging market exposure essentially limited to commercial facilities; these exposures are actively monitored by management. We do not have at-risk exposures in the rest of the world.

Table of Contents

Item 1. Financial Statements

Consolidated Balance Sheets

in millions, except per share data	September 30, 2017 (Unaudited)	December 31, 2016
ASSETS		
Cash and due from banks	$ 562	$ 677
Short-term investments	3,993	2,775
Trading account assets	783	867
Securities available for sale	19,012	20,212
Held-to-maturity securities (fair value: $10,109 and $10,007)	10,276	10,232
Other investments	728	738
Loans, net of unearned income of $734 and $826	86,492	86,038
Less: Allowance for loan and lease losses	(880)	(858)
Net loans	85,612	85,180
Loans held for sale [(a)]	1,341	1,104
Premises and equipment	916	978
Operating lease assets	736	540
Goodwill	2,487	2,446
Other intangible assets	412	384
Corporate-owned life insurance	4,113	4,068
Derivative assets	622	803
Accrued income and other assets	3,744	3,864
Discontinued assets (including $2 and $3 of portfolio loans at fair value, see Note 12)	1,396	1,585
Total assets	$ 136,733	$ 136,453
LIABILITIES		
Deposits in domestic offices:		
NOW and money market deposit accounts	$ 53,734	$ 54,590
Savings deposits	6,366	6,491
Certificates of deposit ($100,000 or more)	6,519	5,483
Other time deposits	4,720	4,698
Total interest-bearing deposits	71,339	71,262
Noninterest-bearing deposits	32,107	32,825
Total deposits	103,446	104,087
Federal funds purchased and securities sold under repurchase agreements	372	1,502
Bank notes and other short-term borrowings	616	808
Derivative liabilities	232	636
Accrued expense and other liabilities	1,717	1,796
Long-term debt	15,100	12,384
Total liabilities	121,483	121,213
EQUITY		
Preferred stock	1,025	1,665
Common shares, $1 par value; authorized 1,400,000,000 shares; issued 1,256,702,081, and 1,256,702,081 shares	1,257	1,257
Capital surplus	6,310	6,385
Retained earnings	10,125	9,378
Treasury stock, at cost (177,663,263 and 177,388,429 shares)	(2,962)	(2,904)
Accumulated other comprehensive income (loss)	(506)	(541)

Key shareholders’ equity	15,249	15,240
Noncontrolling interests	1	—
Total equity	15,250	15,240
Total liabilities and equity	$ 136,733	$ 136,453

(a) Total loans held for sale include real estate — residential mortgage loans held for sale at fair value of $60 million at September 30, 2017, and $62 million at December 31, 2016.

See Notes to Consolidated Financial Statements (Unaudited).

Table of Contents

Consolidated Statements of Income

dollars in millions, except per share amounts	Three months ended September 30,		Nine months ended September 30,	
(Unaudited)	2017	2016	2017	2016
INTEREST INCOME				
Loans	$928	$ 746	$2,753	$ 1,875
Loans held for sale	17	10	39	23
Securities available for sale	91	88	276	237
Held-to-maturity securities	55	30	161	78
Trading account assets	7	4	21	17
Short-term investments	6	7	14	17
Other investments	5	5	12	10
Total interest income	1,109	890	3,276	2,257
INTEREST EXPENSE				
Deposits	72	49	196	114
Federal funds purchased and securities sold under repurchase agreements	—	—	1	—
Bank notes and other short-term borrowings	3	2	12	7
Long-term debt	86	59	228	155
Total interest expense	161	110	437	276
NET INTEREST INCOME	948	780	2,839	1,981
Provision for credit losses	51	59	180	200
Net interest income after provision for credit losses	897	721	2,659	1,781
NONINTEREST INCOME				
Trust and investment services income	135	122	404	341
Investment banking and debt placement fees	141	156	403	325
Service charges on deposit accounts	91	85	268	218
Operating lease income and other leasing gains	16	6	69	41
Corporate services income	54	51	163	154
Cards and payments income	75	66	210	164
Corporate-owned life insurance income	31	29	94	85
Consumer mortgage income	7	6	19	11
Mortgage servicing fees	21	15	54	37
Net gains (losses) from principal investing	3	5	4	16
Other income [(a)]	18	8	134	61
Total noninterest income	592	549	1,822	1,453
NONINTEREST EXPENSE				
Personnel	558	594	1,665	1,425
Net occupancy	74	73	239	193
Computer processing	56	70	171	158
Business services and professional fees	49	76	140	157
Equipment	29	26	83	68
Operating lease expense	24	15	64	42
Marketing	34	32	85	66
FDIC assessment	21	21	62	38
Intangible asset amortization	25	13	69	28
OREO expense, net	3	3	8	6
Other expense	119	159	414	355

Total noninterest expense	992	1,082	3,000	2,536
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	497	188	1,481	698
Income taxes	134	16	386	141
INCOME (LOSS) FROM CONTINUING OPERATIONS	363	172	1,095	557
Income (loss) from discontinued operations, net of taxes $, $1, $3 and, $3 (see note 12)	1	1	6	5
NET INCOME (LOSS)	364	173	1,101	562
Less: Net income (loss) attributable to noncontrolling interests	—	1	1	—
NET INCOME (LOSS) ATTRIBUTABLE TO KEY	$364	$ 172	$1,100	$ 562
Income (loss) from continuing operations attributable to Key common shareholders	$349	$ 165	$1,038	$ 540
Net income (loss) attributable to Key common shareholders	350	166	1,044	545
Per common share:				
Income (loss) from continuing operations attributable to Key common shareholders	$.32	$ .17	$.96	$ .61
Income (loss) from discontinued operations, net of taxes	—	—	.01	.01
Net income (loss) attributable to Key common shareholders [b]	.32	.17	.97	.62
Per common share — assuming dilution:				
Income (loss) from continuing operations attributable to Key common shareholders	$.32	$ .16	$.95	$ .60
Income (loss) from discontinued operations, net of taxes	—	—	.01	.01
Net income (loss) attributable to Key common shareholders [b]	.32	.17	.96	.61
Cash dividends declared per common share	$.095	$ .085	$.275	$ .245
Weighted-average common shares outstanding (000)	1,073,98[illegible]	982,080	1,075,2[illegible]	860,824
Effect of convertible preferred stock	—	—	—	—
Effect of common share options and other stock awards	15,451	12,580	16,359	8,965
Weighted-average common shares and potential common shares outstanding (000) [c]	1,088,8[illegible]	994,660	1,091,6[illegible]	869,789

(a) For the three months ended September 30, 2017, net securities gains totaled less than $1 million. For the three months ended September 30, 2016, net securities losses totaled $6 million. For the three months ended September 30, 2017, and September 30, 2016, we did not have any impairment losses related to securities.

(b) EPS may not foot due to rounding.

(c) Assumes conversion of common share options and other stock awards and/or convertible preferred stock, as applicable.

See Notes to Consolidated Financial Statements (Unaudited).

Table of Contents

Consolidated Statements of Comprehensive Income

in millions	Three months ended September 30,		Nine months ended September 30,	
(Unaudited)	2017	2016	2017	2016
Net income (loss)	$364	$173	$1,101	$562
Other comprehensive income (loss), net of tax:				
Net unrealized gains (losses) on securities available for sale, net of income taxes of $0, ($18), $24, and $93	—	(28)	40	159
Net unrealized gains (losses) on derivative financial instruments, net of income taxes of ($6), ($24), ($16), and $32	(10)	(41)	(27)	53
Foreign currency translation adjustments, net of income taxes of $4, ($1), $8, and $3	7	(2)	14	5
Net pension and postretirement benefit costs, net of income taxes of $1, $1, $4, and $6	3	3	8	6
Total other comprehensive income (loss), net of tax	—	(68)	35	223
Comprehensive income (loss)	364	105	1,136	785
Less: Comprehensive income attributable to noncontrolling interests	—	1	1	—
Comprehensive income (loss) attributable to Key	$364	$104	$1,135	$785

See Notes to Consolidated Financial Statements (Unaudited).

Table of Contents

Consolidated Statements of Changes in Equity

	Key Shareholders' Equity								
dollars in millions, except per share amounts (Unaudited)	Preferred Shares Outstanding (000)	Common Shares Outstanding (000)	Preferred Stock	Common Shares	Capital Surplus	Retained Earnings	Treasury Stock, at Cost	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests
BALANCE AT DECEMBER 31, 2015	2,900	835,751	$ 290	$ 1,017	$ 3,922	$ 8,922	$ (3,000)	$ (405)	$ 13
Net income (loss)						562			—
Other comprehensive income (loss):									
Net unrealized gains (losses) on securities available for sale, net of income taxes of $93								159	
Net unrealized gains (losses) on derivative financial instruments, net of income taxes of $32								53	
Foreign currency translation adjustments, net of income taxes of $3								5	
Net pension and postretirement benefit costs, net of income taxes of $6								6	
Deferred compensation					(8)				
Cash dividends declared on common shares ($.245 per share)						(207)			
Cash dividends declared on Noncumulative Series A Preferred Stock ($5.8125 per share)						(17)			
Common shares issued		239,735		240	2,591				
Common shares repurchased		(6,122)					(73)		
Issuance of Preferred Stock	14,021		875		(6)				
Common shares reissued (returned) for stock options and other employee benefit plans		12,691			(140)		210		
Net contribution from (distribution to) noncontrolling interests									(11)
BALANCE AT SEPTEMBER 30, 2016	16,921	1,082,055	$ 1,165	$ 1,257	$ 6,359	$ 9,260	$ (2,863)	$ (182)	$ 2
BALANCE AT DECEMBER 31, 2016	17,421	1,079,314	$ 1,665	$ 1,257	$ 6,385	$ 9,378	$ (2,904)	$ (541)	$ —
Net income (loss)						1,100			1

Other comprehensive income (loss):								
Net unrealized gains (losses) on securities available for sale, net of income taxes of $24							40	
Net unrealized gains (losses) on derivative financial instruments, net of income taxes of ($16)							(27)	
Foreign currency translation adjustments, net of income taxes of $8							14	
Net pension and postretirement benefit costs, net of income taxes of $4							8	
Deferred compensation				11				
Cash dividends declared on common shares ($.275 per share)					(296)			
Cash dividends declared on Noncumulative Series A Preferred Stock ($1.9375 per share)					(6)			
Cash dividends declared on Noncumulative Series C Preferred Stock ($.539063 per share)					(7)			
Cash dividends declared on Noncumulative Series D Preferred Stock ($37.50 per depository share)					(20)			
Cash dividends declared on Noncumulative Series E Preferred Stock ($1.161199 per depositary share)					(24)			
Open market common share repurchases		(25,564)				(466)		
Employee equity compensation program common share repurchases		(3,479)				(65)		
Series A Preferred Stock exchanged for common shares	(2,900)	20,568	(290)	(49)		338		
Redemption of Series C Preferred Stock	(14,000)		(350)					
Common shares reissued (returned) for stock options and other employee benefit plans		8,200		(37)		135		
Net contribution from (distribution to) noncontrolling interests								—

BALANCE AT SEPTEMBER 30, 2017	521	1,079,039	$ 1,025	$ 1,257	$ 6,310	$ 10,125	$ (2,962)	$ (506)	$ 1

See Notes to Consolidated Financial Statements (Unaudited).

Table of Contents

Consolidated Statements of Cash Flows

in millions	Nine months ended September 30,	
(Unaudited)	2017	2016
OPERATING ACTIVITIES		
Net income (loss)	$1,101	$562
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Provision for credit losses	180	200
Depreciation and amortization expense, net	301	293
Accretion of acquired loans	171	—
Increase in cash surrender value of corporate-owned life insurance	(85)	(76)
Stock-based compensation expense	74	66
FDIC reimbursement (payments), net of FDIC expense	(2)	7
Deferred income taxes (benefit)	134	(63)
Proceeds from sales of loans held for sale	8,109	5,181
Originations of loans held for sale, net of repayments	(8,287)	(5,516)
Net losses (gains) on sales of loans held for sale	(111)	(92)
Net losses (gains) from principal investing	(4)	(16)
Net losses (gains) and writedown on OREO	3	3
Net losses (gains) on leased equipment	2	10
Net securities losses (gains)	(1)	6
Net losses (gains) on sales of fixed assets	16	13
Net decrease (increase) in trading account assets	84	(138)
Other operating activities, net	(606)	420
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	1,079	860
INVESTING ACTIVITIES		
Cash received (used) in acquisitions, net of cash acquired	(74)	(481)
Net decrease (increase) in short-term investments, excluding acquisitions	(1,218)	(509)
Purchases of securities available for sale	(2,725)	(4,203)
Proceeds from sales of securities available for sale	914	4,248
Proceeds from prepayments and maturities of securities available for sale	3,038	2,867
Proceeds from prepayments and maturities of held-to-maturity securities	1,350	1,048
Purchases of held-to-maturity securities	(1,395)	(5,150)
Purchases of other investments	(78)	(28)
Proceeds from sales of other investments	99	204
Proceeds from prepayments and maturities of other investments	2	3
Net decrease (increase) in loans, excluding acquisitions, sales and transfers	(896)	(2,501)
Proceeds from sales of portfolio loans	129	100
Proceeds from corporate-owned life insurance	40	24
Purchases of premises, equipment, and software	(56)	(79)
Proceeds from sales of premises and equipment	—	—
Proceeds from sales of OREO	37	13
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	(833)	(4,444)
FINANCING ACTIVITIES		
Net increase (decrease) in deposits, excluding acquisitions	(641)	4,147
Net increase (decrease) in short-term borrowings	(1,322)	(2,193)
Net proceeds from issuance of long-term debt	2,850	2,078
Payments on long-term debt	(43)	(533)

Issuance of preferred shares	—	519
Open market common share repurchases	(466)	(73)
Employee equity compensation program common share repurchases	(65)	—
Redemption of Preferred Stock Series C	(350)	—
Net proceeds from reissuance of common shares	29	5
Cash dividends paid	(353)	(224)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(361)	3,726
NET INCREASE (DECREASE) IN CASH AND DUE FROM BANKS	(115)	142
CASH AND DUE FROM BANKS AT BEGINNING OF PERIOD	677	607
CASH AND DUE FROM BANKS AT END OF PERIOD	$562	$749
Additional disclosures relative to cash flows:		
Interest paid	$442	$308
Income taxes paid (refunded)	3	68
Noncash items:		
Common stock issued to acquire First Niagara	—	$2,831
Preferred stock issued to acquire First Niagara	—	350
Reduction of secured borrowing and related collateral	$33	59
Loans transferred to portfolio from held for sale	93	8
Loans transferred to held for sale from portfolio	41	32
Loans transferred to OREO	29	15

See Notes to Consolidated Financial Statements (Unaudited).

Notes to Consolidated Financial Statements (Unaudited)
1. Basis of Presentation and Accounting Policies

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

The consolidated financial statements include any voting rights entities in which we have a controlling financial interest. In accordance with the applicable accounting guidance for consolidations, we consolidate a VIE if we have: (i) a variable interest in the entity; (ii) the power to direct activities of the VIE that most significantly affect the entity's economic performance; and (iii) the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the VIE (i.e., we are considered to be the primary beneficiary). Variable interests can include equity interests, subordinated debt, derivative contracts, leases, service agreements, guarantees, standby letters of credit, loan commitments, and other contracts, agreements, and financial instruments. See Note 10 ("Variable Interest Entities") for information on our involvement with VIEs.

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

We believe that the unaudited consolidated interim financial statements reflect all adjustments of a normal recurring nature and disclosures that are necessary for a fair presentation of the results for the interim periods presented. The results of operations for the interim period are not necessarily indicative of the results of operations to be expected for the full year. The interim financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in our 2016 Form 10-K.

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

Accounting Guidance Adopted in 2017

Consolidation. In October 2016, the FASB issued new accounting guidance that amends the previous consolidation guidance issued in February 2015, to require a decision maker that holds an interest in a VIE through an entity under common control to only consider its proportionate indirect interest in the VIE in determining whether the decision maker is the VIE's primary beneficiary. This new guidance eliminates the requirement that a decision maker treat the common control party's interest in the VIE as if the decision maker held the interest itself, an approach referred to as "full attribution." The new guidance was effective for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us) on a retrospective basis. The adoption of this accounting guidance did not affect our financial condition or results of operations.

Stock-based compensation. In March 2016, the FASB issued new accounting guidance that simplifies the accounting for several aspects of share-based payment transactions, including the related income tax consequences, the classification of awards as either equity or liabilities, and the presentation on the statement of cash flows. This accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us). The method of transition was dependent upon the particular amendment within the new guidance. During the nine months ended September 30, 2017, we recognized $26 million in excess tax benefits within “income taxes” on our income statement that pertained to share-based payment arrangements. Prior to 2017, such excess tax benefits were recorded within “capital surplus” on our balance sheet. Under the new guidance, generally, if our share price increases over an award’s vesting period, the resulting tax windfall will decrease “income taxes.” In a like manner, if our share price decreases over an award’s vesting period, the resulting tax shortfall will increase “income taxes.” This change also removed the impact of the excess tax benefits and deficiencies from the calculation of diluted EPS and is required to be applied on a prospective basis. The adoption of this accounting standard did not materially affect our Consolidated Statements of Cash Flows, nor did it affect retained earnings as of the beginning of the period of adoption. We elected to retain our existing accounting policy of estimating award forfeitures upon the award's grant date.

Equity method investments. In March 2016, the FASB issued new accounting guidance that simplifies the transition to equity method accounting by eliminating the requirement for an investor to make retroactive adjustments to the investment, results of operations, and retained earnings on a step-by-step basis when an investment becomes qualified for equity method accounting. Instead, when an investment qualifies for the equity method due to an increase in ownership or degree of influence, an equity method investor is required to add the cost of acquiring the additional interest to the current basis of the previously held interest and to adopt the equity method of accounting as of the date the investment becomes qualified for the equity method. This accounting guidance became effective prospectively for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us). The adoption of this accounting guidance did not affect our financial condition or results of operations. This guidance will only affect our financial condition or results of operations if there is an applicable change in an investment resulting in the investment qualifying for equity method accounting.

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

Derivatives and hedging. In March 2016, the FASB issued new accounting guidance that clarifies that a change in the counterparty to a derivative instrument that has been designated as a hedging instrument does not, by itself, require dedesignation, but all other hedge accounting criteria must be met. This accounting guidance was effective for interim and annual reporting periods beginning after December 15, 2016 (effective January 1, 2017, for us) and was implemented using a prospective method. The adoption of this accounting guidance did not affect our financial condition or results of operations.

Accounting Guidance Pending Adoption at September 30, 2017

Derivatives and hedging. In August 2017, the FASB issued new accounting guidance to better align hedge accounting with risk management activities. It also reduces the complexity involved in applying hedge accounting. Under this new guidance, the concept of hedge ineffectiveness will be eliminated. Ineffective income generated by cash flow and net investment hedges will be recognized in the same financial reporting period and income statement line item as effective income, so as to reflect the full cost of hedging at one time and in one place. Ineffective income generated by fair value hedges will continue to be reflected in current period earnings; however, it will be recognized in the same income statement line item as effective income. The guidance will also allow any contractually specified variable rate to be designated as the hedged risk in a cash flow hedge.

With respect to fair value hedges of interest rate risk, the guidance will allow changes in the fair value of the hedged item to be calculated solely using changes in the benchmark interest rate component of the instrument's total contractual coupon cash flows. In addition, entities will be able to hedge the portion of a closed portfolio of prepayable assets that are not expected to prepay under the "last-of-layer" method. The guidance will permit for a one-time reclassification of debt securities eligible to be hedged under the "last-of-layer" method from held to maturity to available for sale upon adoption. Partial-term fair value hedges will also be allowed.

This guidance is effective for interim and annual reporting periods beginning after December 15, 2018 (effective January 1, 2019, for us). The guidance should be applied on a modified retrospective basis to existing hedge relationships as of the adoption date. Accordingly, a cumulative-effect adjustment will be made to AOCI so that the adjusted amount represents the cumulative change in the hedging instrument's fair value less any amounts that should have been recognized in earnings under the new accounting model. The corresponding adjustment will be made to opening retained earnings as of the most recent period presented as of the adoption date. Early adoption is permitted, including in interim periods. We are currently evaluating early adoption of this guidance as well as the impact it may have on our financial condition and results of operations.

Compensation. In May 2017, the FASB issued new accounting guidance that clarifies when changes to terms and conditions for share-based payment awards should be accounted for as modifications. According to the new guidance, entities should apply the modification guidance unless the fair value of the modified award is the same as

Table of Contents

the fair value of the original award immediately before modification, the vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before modification, and the classification of the modified award (as equity or liability instrument) is the same as the classification of the original award immediately before modification. This accounting guidance is effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us). The guidance should be applied on a prospective basis. Early adoption is permitted, including in interim periods. The adoption of this guidance is not expected to have a material impact on our financial condition or results of operations.

Receivables. In March 2017, the FASB issued new accounting guidance that shortens the amortization period to the earliest call date for certain callable debt securities held at a premium. Securities held at a discount will continue to be amortized to maturity. This accounting guidance is effective for interim and annual reporting periods beginning after December 15, 2018 (effective January 1, 2019, for us). The guidance should be applied on a modified retrospective basis using a cumulative-effect adjustment. Early adoption is permitted. The adoption of this guidance is not expected to have a material impact on our financial condition or results of operations.

Compensation. In March 2017, the FASB issued new accounting guidance that requires service cost to be included in the same line item as certain other compensation costs related to services rendered by employees. We record compensation costs under personnel expense on the income statement. Other elements of net benefit cost should be presented separately. This accounting guidance is effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us). The guidance should be applied on a retrospective basis. Early adoption is permitted within the first interim period if the entity issues interim financial statements. The adoption of this guidance will result in a reclassification of certain net benefit cost components from personnel expense to other expense on the income statement. There will be no material impact to our financial condition or results of operations.

Other income. In February 2017, the FASB issued new accounting guidance that clarifies the scope of asset derecognition guidance and accounting for partial sales of nonfinancial assets. The guidance clarifies that financial assets may be within scope of the derecognition guidance if they are promised to a counterparty in a contract and substantially all the fair value of the assets in the contract are concentrated in nonfinancial assets, which are collectively referred to as in substance nonfinancial assets. The guidance requires entities to derecognize a nonfinancial asset or in substance nonfinancial asset when a counterparty obtains controls of it and, in a partial sale transaction, when it does not have a controlling financial interest in the legal entity that holds the asset. This accounting guidance is effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us). The guidance may be applied on a retrospective or modified retrospective basis. Early adoption is permitted for interim and annual reporting periods beginning after December 15, 2016. The adoption of this guidance is not expected to have a material impact on our financial condition or results of operations.

Goodwill and other intangibles. In January 2017, the FASB issued new accounting guidance that simplifies the test for goodwill impairment by eliminating the second step of the current two-step method. Under the new guidance, entities will compare the fair value of a reporting unit with its carrying amount. If the carrying amount exceeds the reporting unit's fair value, the entity is required to recognize an impairment charge for this amount. Current guidance requires an entity to proceed to a second step, whereby the entity would determine the fair value of its assets and liabilities. The new method applies to all reporting units. The performance of a qualitative assessment is still allowable. This accounting guidance is effective prospectively for interim and annual reporting periods beginning after December 15, 2019 (effective January 1, 2020, for us). Early adoption is permitted. The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

Business combinations. In January 2017, the FASB issued accounting guidance that clarifies the definition of a business and removes the requirement for a market participant to consider whether it could replace missing elements in an integrated set of assets and activities. The guidance states that if substantially all of the fair value of the assets acquired or disposed of is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. This accounting guidance will be effective for annual and interim reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us) and should be implemented using a prospective approach. Early application is allowed for transactions for which the acquisition date occurs before the issuance date or effective date of the amendments, as long as the transaction has not been reported in financial statements that have been issued or made available for issuance, and for transactions in which a subsidiary is

Table of Contents

deconsolidated or a group of assets is derecognized that occurs before the issuance date or effective date of the amendments, as long as the transaction has not been reported in financial statements that have been issued or made available for issuance.

Statement of cash flows. In November 2016, the FASB issued accounting guidance requiring restricted cash and restricted cash equivalents to be included with other cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts presented on the statement of cash flows. This accounting guidance will be effective for annual and interim reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us) and should be implemented using a retrospective approach. Early adoption is permitted. The adoption of this accounting guidance is not expected to have a material effect on the presentation of our Consolidated Statements of Cash Flows, as Key does not hold material balances of restricted cash and restricted cash equivalents.

Income taxes. In October 2016, the FASB issued accounting guidance requiring an entity to recognize any deferred taxes from an intra-entity transfer of an asset other than inventory when the transfer occurs. This accounting guidance will be effective for annual and interim reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us) and should be implemented using a modified retrospective approach. Early adoption is permitted but only as of the beginning of an annual reporting period for which financial statements have not yet been issued. The adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

Statement of cash flows. In August 2016, the FASB issued new accounting guidance that clarifies how cash receipts and cash payments in certain transactions should be presented and classified in the statement of cash flows. These specific transactions include, but are not limited to, debt prepayment or extinguishment costs, contingent considerations made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, and distributions from equity method investees. This guidance also clarifies that in instances of cash flows with multiple aspects that cannot be separately identified, classification should be based on the activity that is likely to be the predominant source of or use of cash flow. This accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us) and should be implemented using a retrospective approach. Early adoption is permitted. The adoption of this accounting guidance is not expected to have a material effect on the presentation of our Consolidated Statements of Cash Flows, as Key’s current policies are either already in-line with the clarifications in the updated guidance, or the related cash flows are not material.

Financial instruments. In June 2016, the FASB issued new accounting guidance that changes the methodology for recognizing credit losses related to financial instruments. Under current GAAP, a credit loss is not recognized until it is probable that the loss has been incurred. The new accounting guidance eliminates that threshold and expands the information required for an entity to consider when developing an estimate of expected credit losses, including the use of forecast information. Entities will be required to present financial assets measured on an amortized cost basis at the net amount that is expected to be collected. This new guidance will impact the accounting for our loans, debt securities held to maturity and available for sale, and liabilities for credit losses on unfunded lending-related commitments as well as purchased financial assets with a more-than-insignificant amount of credit deterioration since origination. This accounting guidance will be effective for interim and annual reporting periods beginning after December 15, 2019 (effective January 1, 2020, for us). Early adoption is permitted but only for interim and annual reporting periods beginning after December 15, 2018. This guidance should be implemented using a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective, except for the provisions governing purchased financial assets with credit deterioration and other-than-temporary impairment of debt securities that had been recognized before the effective date. These two provisions must be implemented prospectively. Key has formed a cross-functional implementation working group comprised of teams throughout Key, including finance and credit. The implementation team has developed a high-level project plan, is identifying and researching key interpretive issues, and is in the process of developing models that meet the requirements of the new guidance. The implementation team is also in the process of assessing forecast accuracy and potential macroeconomic factors that will be used to determine the reasonable and supportable forecast period. Key expects that the new guidance will generally result in an increase in its allowance for credit losses, as it will cover credit losses over the full remaining expected life of loans and commitments and will consider future changes in macroeconomic conditions. We are currently evaluating the extent of the increase at the adoption date.

Leases. In February 2016, the FASB issued new accounting guidance that requires a lessee to recognize a liability to make lease payments and a right-of-use asset representing its right to use an underlying asset during the lease

Table of Contents

term for both finance and operating leases. The definition of a lease was modified to exemplify the concept of control over an asset identified in the lease. Lease classification criteria remain substantially similar to criteria in current lease guidance. The guidance defines which payments can be used in determining lease classification. For short-term leases with a term of 12 months or less, lessees can make a policy election not to recognize lease assets and lease liabilities. Lessor accounting is largely unchanged. Leveraged leases that commenced before the effective date of the new guidance are grandfathered. New disclosures are required, and certain practical expedients are allowed upon adoption. This accounting and disclosure guidance will be effective for interim and annual reporting periods beginning after December 15, 2018 (effective January 1, 2019, for us) and should be implemented using the modified retrospective approach. Early adoption is permitted. Key has formed a cross-functional implementation team and has developed a high-level project plan. At December 31, 2016, Key had minimum future rental payments under noncancelable operating leases of $968 million. We are currently evaluating this operating lease population and working to identify our complete lease population, including potential embedded leases. We expect the adoption of this standard to result in additional assets and liabilities, as we will be required to recognize operating leases on our Consolidated Balance Sheet. Other implementation matters to be addressed include, but are not limited to, the determination of the effect on our financial and capital ratios and the quantification of the impact on our financial condition and results of operations.

Financial instruments. In January 2016, the FASB issued new accounting guidance that requires equity investments, except those accounted for under the equity method of accounting or consolidated, to be measured at fair value with changes recognized in net income. If there is no readily determinable fair value, the guidance allows entities the ability to measure investments at cost less impairment, whereby impairment is based on a qualitative assessment. The guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost and changes the presentation of financial assets and financial liabilities on the balance sheet or in the footnotes. If an entity has elected the fair value option to measure liabilities, the new accounting guidance requires the portion of the change in the fair value of a liability resulting from credit risk to be presented in OCI. This accounting and disclosure guidance will be effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us). For the provisions of the guidance that are applicable to us, the accounting will be implemented on a modified retrospective basis though a cumulative-effect adjustment to the balance sheet, except for the guidance related to equity securities without readily determinable fair values, which will be applied on a prospective basis. Except under certain instances, early adoption is not permitted. The adoption of this guidance is not expected to have a material impact on our financial condition or results of operations.

Revenue recognition. In May 2014, the FASB issued new accounting guidance that revises the criteria for determining when to recognize revenue from contracts with customers and expands disclosure requirements. The core principle is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides a five step model to be followed in making this determination. This accounting guidance can be implemented using either a retrospective method or a cumulative-effect approach. This new guidance will be effective for interim and annual reporting periods beginning after December 15, 2017 (effective January 1, 2018, for us). Early adoption is permitted but only for interim and annual reporting periods beginning after December 15, 2016. We have elected to implement this new accounting guidance using a cumulative-effect approach. We have identified the revenue line items within the scope of the new guidance and are currently finalizing our contract testing related to trust and investment services income, investment banking and debt placement fees, service charges on deposit accounts, and cards and payments income. The guidance will change our presentation of certain underwriting and credit and debit card related costs. Underwriting costs will change from a net presentation to a gross expense. Certain credit and debit card related costs will change from a gross presentation to a reduction in revenue. Additionally, we will expand our qualitative disclosures on those revenues within the scope of the new guidance. While the final assessment is still ongoing, the adoption of this accounting guidance is not expected to have a material effect on our financial condition or results of operations.

2. Business Combination

First Niagara

On August 1, 2016 (the "Acquisition Date"), we acquired all of the outstanding common shares of First Niagara, the parent company of First Niagara Bank, for total consideration of approximately $4.0 billion and thereby acquired First Niagara Bank's approximately 390 branch locations across New York, Pennsylvania, Connecticut, and Massachusetts. The merger with First Niagara enabled us to expand in the New England market and into the Pennsylvania market, improve our core deposit base, and add additional scale in our banking operations. The results of First Niagara's operations are included in our consolidated financial statements from the Acquisition Date.

Under the terms of the merger agreement, each outstanding share of First Niagara common stock was converted into the right to receive 0.680 KeyCorp Common Shares and $2.30 in cash, for a total per-share value of $10.26, based on the $11.70 closing price of KeyCorp's stock on July 29, 2016. In the aggregate, First Niagara stockholders received 240 million shares of KeyCorp common stock. Also under the terms of the merger agreement, First Niagara employee stock options and restricted stock awards converted into options to purchase and receive KeyCorp common stock. These options and restricted stock awards had a fair value of $26 million on the Acquisition Date. Our methodology for valuing employee stock options is disclosed in Note 16 ("Stock-Based Compensation") under the heading "Stock Options" on page 179 of our 2016 Form 10-K. Our methodology for valuing restricted stock awards is disclosed in Note 16 ("Stock-Based Compensation") under the heading "Long-Term Incentive Compensation Program" on page 180 of our 2016 Form 10-K.

In addition, at the time of the merger, each share of First Niagara preferred stock, Series B, was converted into the right to receive a share of KeyCorp preferred stock, Series C, a newly created series of KeyCorp preferred stock. Additional information on this series of preferred stock is provided in Note 18 ("Shareholders' Equity") of this report.

On October 7, 2016, First Niagara Bank merged with and into KeyBank, with KeyBank as the surviving entity. Systems and client conversion also occurred during the fourth quarter of 2016 in connection with the bank merger.

The acquisition of First Niagara constituted a business combination and was accounted for under the acquisition method of accounting. Accordingly, the assets acquired, the liabilities assumed, and the consideration paid were recorded at their estimated fair value as of the Acquisition Date.

The following table provides the final purchase price calculation as of the Acquisition Date and the identifiable assets purchased and the liabilities assumed at their fair value. These fair value measurements were based on internal and third-party valuations.

in millions		
Consideration paid:		
KeyCorp common stock issued		$2,831
Cash payments to First Niagara stockholders		811
Exchange of First Niagara preferred stock for KeyCorp preferred stock		350
Total consideration paid		$3,992
Statement of Net Assets Acquired at Fair Value:		
ASSETS		
Cash and due from banks and short-term investments	$620	
Investment securities	9,012	
Other investments	297	
Loans	23,590	
Premises and equipment	245	
Other intangible assets	385	

Accrued income and other assets	1,467	
Total assets	$35,616	
LIABILITIES		
Deposits	$28,994	
Bank notes and other short-term borrowings	2,698	
Accrued expense and other liabilities	490	
Long-term debt	846	
Total liabilities	$33,028	
Net identifiable assets acquired		2,588
Goodwill		$1,404

67

Measurement Period Adjustments

We estimated the fair value of loans acquired from First Niagara by utilizing the discounted cash flow method within the income approach. This methodology aggregates the purchased loans by category and risk rating. Cash flows for each category were determined by estimating future credit losses and the rate of prepayments. Projected monthly cash flows were then discounted to present value based on a market rate for similar loans. There was no carryover of First Niagara's ALLL associated with the loans we acquired. The valuation of the acquired loans was final at June 30, 2017.

Based on the final valuations, we updated our fair values within our June 30, 2017, Consolidated Balance Sheet with a corresponding adjustment to goodwill. There were no measurement period adjustments during the third quarter of 2017.

The amounts reflected in the following table represent the change in the fair values of acquired assets as of June 30, 2017:
in millions

Acquired Asset	Balance Sheet Line Item	Provisional Estimate	Final	Increase (Decrease)
Loans	Loans	$ 23,645	$23,590	$ (55)
Tax adjustment on previous fair value measurement (a)	Accrued income and other assets	1,449	1,467	18
Unfunded lending-related commitments	Accrued expense and other liabilities	67	65	(2)
Deferred compensation (a)	Accrued expense and other liabilities	39	41	2

(a) The fair value adjustment did not have any impact on the income statement for the three and six months ended June 30, 2017.

The finalization of the fair values also impacted various income statement line items on the Consolidated Statements of Income. The amounts shown in the table below represent the increase (decrease) in the respective line items for the previous reporting period had the final fair value been recorded at the Acquisition Date for the nine months ended September 30, 2017.

in millions

Acquired Asset	Income Statement Line Item	Portion Related to Previous Reporting Period (a)
Loans	Interest income	$ 42
Loans	Provision for credit losses	1
Loans	Other noninterest income	(3)
Unfunded lending-related commitments	Other noninterest income	(4)

(a) Represents the change in amount that should have been reported compared to what was actually reported in the December 31, 2016, Consolidated Statements of Income.

Intangible assets consisted of the core deposit intangible, the commercial purchased credit card relationships, the consumer purchased credit card relationships, and other intangible assets. The core deposit intangible asset of $356 million recognized as part of the First Niagara merger is being amortized over its estimated useful life of approximately ten years utilizing an accelerated method. The commercial purchased credit card relationships recognized as part of the First Niagara merger are being amortized over their estimated useful life of approximately six years utilizing an accelerated method. The consumer purchased credit card relationships recognized as part of the First Niagara merger are being amortized over their estimated useful life of approximately nine years utilizing an accelerated method.

Goodwill of $1.4 billion was recorded as a result of the transaction and is not amortized for book purposes. Of this total, $1.1 billion of goodwill was assigned to our Key Community Bank segment and $280 million of goodwill was assigned to our Key Corporate Bank segment. The goodwill recorded is not deductible for tax purposes. The following table shows the changes in the carrying amount of goodwill by reporting unit.

in millions	Key Community Bank	Key Corporate Bank	Total
BALANCE AT DECEMBER 31, 2015	$ 979	$ 81	$1,060
Acquisition of First Niagara	1,109	277	1,386
BALANCE AT DECEMBER 31, 2016	2,088	358	2,446
Tax adjustment on previous fair value measurements	(15)	(4)	(19)
Loan adjustment on previous fair value measurements	30	7	37
BALANCE AT JUNE 30, 2017	$ 2,103	$ 361	$2,464

Certificates of deposit were valued by projecting out the expected cash flows based on the contractual terms of the certificates of deposit. The fair values of savings and transaction deposit accounts acquired from First Niagara were assumed to approximate the carrying value as these accounts have no stated maturity and are payable on demand. These cash flows were discounted based on a market rate for a certificate of deposit with a corresponding maturity.

Direct acquisition costs related to the First Niagara acquisition were expensed as incurred and amounted to less than $1 million for the nine months ended September 30, 2017. These direct acquisition costs are part of our total merger-related charges.

The following table presents unaudited pro forma information as if the acquisition of First Niagara had occurred on January 1, 2015. This pro forma information gives effect to certain adjustments, including purchase accounting fair value adjustments, amortization of core deposit and other intangibles, and related income tax effects. Merger-related charges related to the First Niagara merger that we incurred during the nine months ended September 30, 2016, are not reflected in the unaudited pro forma amounts. The pro forma information does not necessarily reflect the results of operations that would have occurred had KeyCorp merged with First Niagara at the beginning of 2015. Cost savings are also not reflected in the unaudited pro forma amounts for the nine months ended September 30, 2016.

in millions	Pro forma Nine months ended September 30, 2016
Net interest income (TE)	$ 2,674
Noninterest income	1,625
Net income (loss) attributable to common shareholders	849

For information on the Cain Brothers & Company, LLC, HelloWallet Holdings, Inc., and Key Merchant Services, LLC acquisitions, see note 12 (“Acquisition, Divestiture, and Discontinued Operations”).

Table of Contents

3. Earnings Per Common Share

Basic earnings per share is the amount of earnings (adjusted for dividends declared on our preferred stock) available to each common share outstanding during the reporting periods. Diluted earnings per share is the amount of earnings available to each common share outstanding during the reporting periods adjusted to include the effects of potentially dilutive common shares. Potentially dilutive common shares include stock options and other stock-based awards. Potentially dilutive common shares are excluded from the computation of diluted earnings per share in the periods where the effect would be antidilutive.

On March 20, 2017, all outstanding Series A Preferred Stock was converted into KeyCorp common shares. Prior to this conversion, for diluted earnings per share, net income available to common shareholders could have been affected by the conversion of our convertible Series A Preferred Stock. Where the effect of this conversion would have been dilutive, net income available to common shareholders was adjusted by the amount of preferred dividends associated with our Series A Preferred Stock.

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

	Three months ended September 30,		Nine months ended September 30,	
dollars in millions, except per share amounts	2017	2016	2017	2016
EARNINGS				
Income (loss) from continuing operations	$363	$ 172	$1,095	$ 557
Less: Net income (loss) attributable to noncontrolling interests	—	1	1	—
Income (loss) from continuing operations attributable to Key	363	171	1,094	557
Less: Dividends on Preferred Stock	14	6	56	17
Income (loss) from continuing operations attributable to Key common shareholders	349	165	1,038	540
Income (loss) from discontinued operations, net of taxes [(a)]	1	1	6	5
Net income (loss) attributable to Key common shareholders	$350	$ 166	$1,044	$ 545
WEIGHTED-AVERAGE COMMON SHARES				
Weighted-average common shares outstanding (000)	1,073,392	932,080	1,075,296	860,824
Effect of convertible preferred stock	—	—	—	—
Effect of common share options and other stock awards	15,451	12,580	16,359	8,965
Weighted-average common shares and potential common shares outstanding (000) [(b)]	1,088,843	944,660	1,091,655	869,789
EARNINGS PER COMMON SHARE				
Income (loss) from continuing operations attributable to Key common shareholders	$.32	$ .17	$.96	$ .61
Income (loss) from discontinued operations, net of taxes [(a)]	—	—	.01	.01
Net income (loss) attributable to Key common shareholders [(c)]	.32	.17	.97	.62
Income (loss) from continuing operations attributable to Key common shareholders — assuming dilution	$.32	$ .16	$.95	$ .60
Income (loss) from discontinued operations, net of taxes [(a)]	—	—	.01	.01
Net income (loss) attributable to Key common shareholders — assuming dilution [(c)]	.32	.17	.96	.61

(a) In September 2009, we decided to discontinue the education lending business conducted through Key Education Resources, the education payment and financing unit of KeyBank. As a result of this decision, we have accounted for this business as a discontinued operation. For further discussion regarding the income (loss) from discontinued operations, see Note 12 ("Acquisition, Divestiture, and Discontinued Operations").

(b) Assumes conversion of common share options and other stock awards and/or convertible preferred stock, as applicable.

(c) EPS may not foot due to rounding.

Table of Contents

4. Loans and Loans Held for Sale

in millions	September 30, 2017	December 31, 2016
Commercial and industrial [(a)]	$ 41,147	$ 39,768
Commercial real estate:		
Commercial mortgage	14,929	15,111
Construction	1,954	2,345
Total commercial real estate loans	16,883	17,456
Commercial lease financing [(b)]	4,716	4,685
Total commercial loans	62,746	61,909
Residential — prime loans:		
Real estate — residential mortgage	5,476	5,547
Home equity loans	12,238	12,674
Total residential — prime loans	17,714	18,221
Consumer direct loans	1,789	1,788
Credit cards	1,045	1,111
Consumer indirect loans	3,198	3,009
Total consumer loans	23,746	24,129
Total loans [(c), (d)]	$ 86,492	$ 86,038

(a) Loan balances include $118 million and $116 million of commercial credit card balances at September 30, 2017, and December 31, 2016, respectively.

(b) Commercial lease financing includes receivables held as collateral for a secured borrowing of $31 million and $68 million at September 30, 2017, and December 31, 2016, respectively. Principal reductions are based on the cash payments received from these related receivables. Additional information pertaining to this secured borrowing is included in Note 19 (“Long-Term Debt”) beginning on page 191 of our 2016 Form 10-K.

(c) At September 30, 2017, total loans include purchased loans of $16.7 billion of which $783 million were PCI loans. At December 31, 2016, total loans include purchased loans of $21 billion, of which $865 million were PCI loans.

(d) Total loans exclude loans of $1.4 billion at September 30, 2017, and $1.6 billion at December 31, 2016, related to the discontinued operations of the education lending business. Additional information pertaining to these loans is provided in Note 12 (“Acquisition, Divestiture, and Discontinued Operations”).

Our loans held for sale are summarized as follows:

in millions	September 30, 2017	December 31, 2016
Commercial and industrial	$ 34	$ 19
Real estate — commercial mortgage	1,246	1,022
Real estate — construction	—	1
Commercial lease financing	1	—
Real estate — residential mortgage [(a)]	60	62
Total loans held for sale	$ 1,341	$ 1,104

(a) Real estate — residential mortgage loans held for sale are held at fair value at September 30, 2017, and December 31, 2016. The fair value option was elected for real estate — residential mortgage loans held for sale during the third quarter of 2016 with the First Niagara acquisition. The contractual amount due on these loans totaled $60 million at September 30, 2017, and $62 million at December 31, 2016. Changes in fair value are recorded in “Consumer mortgage income” on the income statement. Additional information regarding residential mortgage loans held for sale fair value methodology is provided in Note 6 ("Fair Value Measurements").

Our quarterly summary of changes in loans held for sale is provided below:

in millions	September 30, 2017	June 30, 2017	December 31, 2016
Balance at beginning of the period	$ 1,743	$ 1,384	$ 1,137
New originations	2,855	2,876	2,846
Transfers from (to) held to maturity, net	(63)	(7)	11
Loan sales	(3,191)	(2,507)	(2,889)
Loan draws (payments), net	(3)	(3)	(1)
Balance at end of period [(a)]	$ 1,341	$ 1,743	$ 1,104

(a) Total loans held for sale include real estate — residential mortgage loans held for sale at fair value of $60 million at September 30, 2017, $63 million at June 30, 2017, and $62 million at December 31, 2016.

71

Table of Contents

5. Asset Quality

We assess the credit quality of the loan portfolio by monitoring net credit losses, levels of nonperforming assets, delinquencies, and credit quality ratings as defined by management. Nonperforming loans are loans for which we do not accrue interest income, and include commercial and consumer loans and leases, as well as current year TDRs and nonaccruing TDR loans from prior years. Nonperforming assets include nonperforming loans, nonperforming loans held for sale, OREO, and other nonperforming assets. Nonimpaired acquired loans are placed on nonaccrual status and reported as nonperforming or past due using the same criteria applied to the originated portfolio. PCI loans cannot be classified as nonperforming loans or TDRs.

Our nonperforming assets and past due loans were as follows:

in millions	September 30, 2017	December 31, 2016
Total nonperforming loans [(a)]	$ 517	$ 625
OREO [(b)]	39	51
Other nonperforming assets	—	—
Total nonperforming assets	$ 556	$ 676
Nonperforming assets from discontinued operations—education lending [(c)]	$ 8	$ 5
TDRs included in nonperforming loans	187	141
TDRs with an allocated specific allowance [(d)]	67	59
Specifically allocated allowance for restructured loans [(e)]	19	27
Accruing loans past due 90 days or more	86	87
Accruing loans past due 30 through 89 days	329	404

(a) Nonperforming loan balances exclude $783 million and $865 million of PCI loans at September 30, 2017, and December 31, 2016, respectively.
(b) Includes carrying value of foreclosed residential real estate of approximately $29 million and $29 million at September 30, 2017 and December 31, 2016, respectively.
(c) Restructured loans of approximately $24 million and $22 million are included in discontinued operations at September 30, 2017, and December 31, 2016, respectively. See Note 12 (“Acquisition, Divestiture, and Discontinued Operations”) for further discussion.
(d) Included in individually impaired loans allocated a specific allowance.
(e) Included in allowance for individually evaluated impaired loans.

We evaluate purchased loans for impairment in accordance with the applicable accounting guidance. Purchased loans that have evidence of deterioration in credit quality since origination and for which it is probable, at acquisition, that all contractually required payments will not be collected are deemed PCI. Several factors are considered when evaluating whether a loan is considered a PCI loan, including the delinquency status of the loan, updated borrower credit status, and updated LTV ratios. In accordance with ASC 310-30, excluded from the purchased impaired loans are leases, revolving credit arrangements, and loans held for sale.

We estimated the fair value of loans acquired from First Niagara by utilizing the discounted cash flow method within the income approach. See Note 2 (“Business Combination”) for further discussion of the fair value methodology used. There was no carryover of First Niagara’s ALLL associated with the loans we acquired.

The excess of a PCI loan’s contractually required payments over the amount of its undiscounted cash flows expected to be collected is referred to as the nonaccretable difference. The nonaccretable difference, which is not accreted into income, reflects estimated future credit losses and uncollectible contractual interest expected to be incurred over the life of the PCI loan or pool. The excess of cash flows expected to be collected over the carrying amount of the PCI loans or pools is referred to as the accretable yield. This amount is accreted into interest income over the remaining life of the PCI loans or pools using the level yield method.

Over the life of PCI loans or pools, Key evaluates the remaining contractually required payments receivable and estimates cash flows expected to be collected. Contractually required payments receivable may increase or decrease for a variety of reasons, such as, when the contractual terms of the loan agreement are modified, when interest rates on variable rate loans change, or when principal and/or interest payments are received. Cash flows expected to be collected on PCI loans are estimated by incorporating several primary assumptions similar to the initial estimate of fair value. These primary assumptions include probability of default, loss given default, and prepayment rate. Increases in expected cash flows of PCI loans or pools subsequent to acquisition are recognized prospectively through adjustment of the yield on the loans or pools over its remaining life, while decreases in expected cash flows are recognized as impairment through a provision for credit losses and an increase in the ALLL.

Table of Contents

The difference between the fair value of a nonimpaired acquired loan and contractual amounts due at the Acquisition Date is accreted into income over the estimated life of the loan or pool. Contractually required payments represent the total undiscounted amount of all uncollected principal and interest payments.

The following table presents the PCI loans receivable balance at the First Niagara Acquisition Date:

August 1, 2016 in millions	PCI
Contractual required payments receivable	$1,434
Nonaccretable difference	173
Expected cash flows	1,261
Accretable yield	172
Fair value	$1,089

At the First Niagara Acquisition Date, the contractual required payments receivable on the purchased non-impaired loans totaled $22.5 billion, with a corresponding estimated fair value of $22.0 billion. The estimated cash flows not expected to be collected at the Acquisition Date were $500 million. These amounts do not include loans held for sale and the loans that were divested as part of the 18 branches that were sold on September 9, 2016.

We have PCI loans from two seperate acquisitions, one in 2012 and one during the third quarter of 2016. The following tables present the roll-forward of the accretable yield and the beginning and ending outstanding unpaid principal balance and carrying amount of all PCI loans for the three and nine months ended September 30, 2017, and the twelve months ended December 31, 2016. The rollforward of the accretable yield for the nine months ended September 30, 2017, reflects the impact of prospective purchase accounting adjustments resulting from the finalization of the First Niagara Acquisition Date loan valuation during the second quarter of 2017.

	Three Months Ended September 30, 2017			Nine Months Ended September 30, 2017		
in millions	Accretable Yield	Carrying Amount	Outstanding Unpaid Principal Balance	Accretable Yield	Carrying Amount	Outstanding Unpaid Principal Balance
Balance at beginning of period	$137	$ 812	$ 930	$197	$ 865	$ 1,002
Additions	—			(33)		
Accretion	(12)			(32)		
Net reclassifications from nonaccretable to accretable	30			19		
Payments received, net	(5)			(1)		
Disposals	—			—		
Balance at end of period	$150	$ 783	$ 854	$150	$ 783	$ 854

	Twelve Months Ended December 31, 2016		
in millions	Accretable Yield	Carrying Amount	Outstanding Unpaid Principal Balance
Balance at beginning of period	$5	$ 11	$ 17
Additions	205		

Accretion	(29)		
Net reclassifications from nonaccretable to accretable	35		
Payments received, net	(19)		
Disposals	—		
Balance at end of period	$197	$ 865	$ 1,002

At September 30, 2017, the approximate carrying amount of our commercial nonperforming loans outstanding represented 79% of their original contractual amount owed, total nonperforming loans outstanding represented 83% of their original contractual amount owed, and nonperforming assets in total were carried at 83% of their original contractual amount owed. At September 30, 2017, our 20 largest nonperforming loans totaled $154 million, representing 30% of total loans on nonperforming status.

Nonperforming loans and loans held for sale reduced expected interest income by $6 million and $18 million for the three and nine months ended September 30, 2017, respectively, and $7 million and $19 million for the three and nine months ended September 30, 2016, respectively.

Table of Contents

The following tables set forth a further breakdown of individually impaired loans as of September 30, 2017, and December 31, 2016:

September 30, 2017 in millions	Recorded Investment [(a)]	Unpaid Principal Balance [(b)]	Specific Allowance
With no related allowance recorded:			
Commercial and industrial	$ 124	$ 148	—
Commercial real estate:			
Commercial mortgage	12	17	—
Total commercial real estate loans	12	17	—
Total commercial loans	136	165	—
Real estate — residential mortgage	18	18	—
Home equity loans	50	49	—
Consumer indirect loans	2	2	—
Total consumer loans	70	69	—
Total loans with no related allowance recorded	206	234	—
With an allowance recorded:			
Commercial and industrial	33	43	$ 7
Commercial real estate:			
Commercial mortgage	—	—	—
Total commercial real estate loans	—	—	—
Total commercial loans	33	43	7
Real estate — residential mortgage	32	32	5
Home equity loans	67	67	7
Consumer direct loans	4	4	—
Credit cards	3	3	—
Consumer indirect loans	31	31	4
Total consumer loans	137	137	16
Total loans with an allowance recorded	170	180	23
Total	$ 376	$ 414	$ 23

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

December 31, 2016 in millions	Recorded Investment [(a)]	Unpaid Principal Balance [(b)]	Specific Allowance
With no related allowance recorded:			
Commercial and industrial	$ 222	$ 301	—
Commercial real estate:			
Commercial mortgage	2	3	—
Total commercial real estate loans	2	3	—
Total commercial loans	224	304	—
Real estate — residential mortgage	20	20	—
Home equity loans	61	61	—
Consumer indirect loans	1	1	—
Total consumer loans	82	82	—

Total loans with no related allowance recorded	306	386	—
With an allowance recorded:			
Commercial and industrial	62	73	$ 17
Commercial real estate:			
Commercial mortgage	4	4	—
Total commercial real estate loans	4	4	—
Total commercial loans	66	77	17
Real estate — residential mortgage	31	31	2
Home equity loans	64	64	18
Consumer direct loans	2	3	—
Credit cards	3	3	—
Consumer indirect loans	29	29	1
Total consumer loans	129	130	21
Total loans with an allowance recorded	195	207	38
Total	$ 501	$ 593	$ 38

(a) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. This amount is a component of total loans on our Consolidated Balance Sheet.

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

Table of Contents

The following table sets forth a further breakdown of the average recorded investment for individually impaired loans reported by Key:

Average Recorded Investment [a]	Three Months Ended September 30,		Nine Months Ended September 30,	
in millions	2017	2016	2017	2016
Commercial and industrial	$ 162	$ 319	$ 221	$ 193
Commercial real estate:				
Commercial mortgage	14	7	8	9
Construction	—	17	—	9
Total commercial real estate loans	14	24	8	18
Total commercial loans	176	343	229	211
Real estate — residential mortgage	49	53	50	54
Home equity loans	118	129	121	126
Consumer direct loans	4	3	3	3
Credit cards	2	3	3	3
Consumer indirect loans	33	33	32	35
Total consumer loans	206	221	209	221
Total	$ 382	$ 564	$ 438	$ 432

(a) The Recorded Investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs. This amount is a component of total loans on our Consolidated Balance Sheet.

Interest income recognized on the outstanding balances of accruing impaired loans totaled $3 million and $9 million for the three and nine months ended September 30, 2017, respectively, and $2 million and $8 million for the three and nine months ended September 30, 2016, respectively.

At September 30, 2017, aggregate restructured loans (accrual and nonaccrual loans) totaled $315 million, compared to $280 million at December 31, 2016. During the three months ended September 30, 2017, we added $20 million in restructured loans, which were offset by $38 million in payments and charge-offs. During the nine months ended September 30, 2017, we added $134 million in restructured loans, which were partially offset by $99 million in payments and charge-offs. During 2016, we added $107 million in restructured loans, which were offset by $107 million in payments and charge-offs.

A further breakdown of TDRs included in nonperforming loans by loan category as of September 30, 2017, follows:

September 30, 2017 dollars in millions	Number of Loans	Pre-modification Outstanding Recorded Investment	Post-modification Outstanding Recorded Investment
LOAN TYPE			
Nonperforming:			
Commercial and industrial	20	$ 105	$ 83
Commercial real estate:			
Commercial mortgage	8	17	12

Total commercial real estate loans	8	17	12
Total commercial loans	28	122	95
Real estate — residential mortgage	303	18	18
Home equity loans	1,145	69	61
Consumer direct loans	55	1	1
Credit cards	250	1	1
Consumer indirect loans	724	14	11
Total consumer loans	2,477	103	92
Total nonperforming TDRs	2,505	225	187
Prior-year accruing:[(a)]			
Commercial and industrial	5	30	13
Total commercial loans	5	30	13
Real estate — residential mortgage	499	32	32
Home equity loans	1,223	72	57
Consumer direct loans	24	1	1
Credit cards	480	3	2
Consumer indirect loans	321	33	23
Total consumer loans	2,547	141	115
Total prior-year accruing TDRs	2,552	171	128
Total TDRs	5,057	$ 396	$ 315

(a) Represents TDRs that were restructured prior to January 1, 2017, and are fully accruing.

Table of Contents

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

December 31, 2016 dollars in millions	Number of Loans	Pre-modification Outstanding Recorded Investment	Post-modification Outstanding Recorded Investment
LOAN TYPE			
Nonperforming:			
Commercial and industrial	18	$ 91	$ 50
Commercial real estate:			
Commercial mortgage	7	2	1
Total commercial real estate loans	7	2	1
Total commercial loans	25	93	51
Real estate — residential mortgage	264	16	16
Home equity loans	1,199	77	69
Consumer direct loans	32	1	—
Credit cards	336	2	2
Consumer indirect loans	124	4	3
Total consumer loans	1,955	100	90
Total nonperforming TDRs	1,980	193	141
Prior-year accruing: [(a)]			
Commercial and Industrial	5	30	16
Total commercial loans	5	30	16
Real estate — residential mortgage	477	35	35
Home equity loans	1,231	70	57
Consumer direct loans	35	2	2
Credit cards	410	3	1
Consumer indirect loans	377	56	28
Total consumer loans	2,530	166	123
Total prior-year accruing TDRs	2,535	196	139
Total TDRs	4,515	$ 389	$ 280

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

We classify loan modifications as TDRs when a borrower is experiencing financial difficulties and we have granted a concession without commensurate financial, structural, or legal consideration. Acquired loans that were previously modified in a TDR are no longer classified as TDRs at the Acquisition Date. An acquired loan may only be classified as a TDR if a modification meeting the above TDR criteria is performed after the Acquisition Date. PCI loans cannot be classified as TDRs. All commercial and consumer loan TDRs, regardless of size, are individually evaluated for impairment to determine the probable loss content and are assigned a specific loan loss allowance. This designation has the effect of moving the loan from the general reserve methodology (i.e., collectively evaluated) to the specific reserve methodology (i.e., individually evaluated) and may impact the ALLL through a charge-off or increased loan loss provision. These components affect the ultimate allowance level. Additional information regarding TDRs for discontinued operations is provided in Note 12 (“Acquisition, Divestiture, and Discontinued Operations”).

Commercial loan TDRs are considered defaulted when principal and interest payments are 90 days past due. Consumer loan TDRs are considered defaulted when principal and interest payments are more than 60 days past due. During the three months ended September 30, 2017, there were no commercial loan TDRs and 45 consumer loan

TDRs with a combined recorded investment of $1 million that experienced payment defaults after modifications resulting in TDR status during 2016. During the three months ended September 30, 2016, there were no commercial loan TDRs and 23 consumer loan TDRs with a combined recorded investment of $1 million that experienced payment defaults after modifications resulting in TDR status during 2015.

During the nine months ended September 30, 2017, there were no commercial loan TDRs and 100 consumer loan TDRs with a combined recorded investment of $3 million that experienced payment defaults after modifications resulting in TDR status during 2016. During the nine months ended September 30, 2016, there were no commercial loan TDRs and 153 consumer TDRs with a combined recorded investment of $7 million that experienced payment defaults after modifications resulting in TDR status during 2015.

As TDRs are individually evaluated for impairment under the specific reserve methodology, subsequent defaults do not generally have a significant additional impact on the ALLL. Commitments outstanding to lend additional funds to borrowers whose loan terms have been modified in TDRs are $12 million and $14 million at September 30, 2017 and December 31, 2016, respectively.

Table of Contents

Our loan modifications are handled on a case-by-case basis and are negotiated to achieve mutually agreeable terms that maximize loan collectability and meet the borrower's financial needs. Our concession types are primarily interest rate reductions, forgiveness of principal, and other modifications. The commercial TDR other concession category includes modification of loan terms, covenants, or conditions. The consumer TDR other concession category primarily includes those borrowers' debts that are discharged through Chapter 7 bankruptcy and have not been formally re-affirmed. At September 30, 2017, and December 31, 2016, the recorded investment of consumer residential mortgage loans in the process of foreclosure was approximately $140 million and $141 million, respectively.

The following table shows the post-modification outstanding recorded investment by concession type for our commercial and consumer accruing and nonaccruing TDRs that occurred during the three and nine months ended September 30, 2017, and September 30, 2016.

	Three Months Ended September 30,		Nine Months Ended September 30,	
in millions	2017	2016	2017	2016
Commercial loans:				
Interest rate reduction	$ 7	$ 10	$ 56	25
Forgiveness of principal	—	—	21	—
Other	—	23	9	$ 26
Total	$ 7	$ 33	$ 86	$ 51
Consumer loans:				
Interest rate reduction	$ 3	$ 2	$ 10	$ 8
Forgiveness of principal	—	—	—	—
Other	8	5	21	19
Total	$ 11	$ 7	$ 31	$ 27
Total commercial and consumer TDRs	$ 18	$ 40	$ 117	$ 78
Total loans	86,492	85,528	86,492	85,528

Our policies for determining past due loans, placing loans on nonaccrual, applying payments on nonaccrual loans, and resuming accrual of interest for our commercial and consumer loan portfolios are disclosed in Note 1 ("Summary of Significant Accounting Policies") under the heading "Nonperforming Loans" beginning on page 108 of our 2016 Form 10-K.

The following aging analysis of past due and current loans as of September 30, 2017, and December 31, 2016, provides further information regarding Key's credit exposure.

Aging Analysis of Loan Portfolio [(a)]

September 30, 2017 in millions	Current	30-59 Days Past Due [(b)]	60-89 Days Past Due [(b)]	90 and Greater Days Past Due [(b)]	Non-performing Loans	Total Past Due and Non-performing Loans	Purchased Credit Impaired	Total Loans [(c), (d)]
LOAN TYPE								
Commercial and industrial	$40,758	$ 56	$ 47	$ 24	$ 169	$ 296	$ 93	$41,147
Commercial real estate:								
Commercial mortgage	14,550	39	9	26	30	104	275	14,929
Construction	1,908	20	—	—	2	22	24	1,954

Total commercial real estate loans	16,458	59	9	26	32	126	299	16,883
Commercial lease financing	4,685	14	3	3	11	31	—	4,716
Total commercial loans	$61,901	$ 129	$ 59	$ 53	$ 212	$ 453	$ 392	$62,746
Real estate — residential mortgage	$5,028	$ 20	$ 6	$ 3	$ 57	$ 86	$ 362	$5,476
Home equity loans	11,927	33	15	12	227	287	24	12,238
Consumer direct loans	1,759	11	6	5	3	25	5	1,789
Credit cards	1,021	7	5	10	2	24	—	1,045
Consumer indirect loans	3,141	31	7	3	16	57	—	3,198
Total consumer loans	$22,876	$ 102	$ 39	$ 33	$ 305	$ 479	$ 391	$23,746
Total loans	$84,777	$ 231	$ 98	$ 86	$ 517	$ 932	$ 783	$86,492

(a) Amounts in table represent recorded investment and exclude loans held for sale. Recorded investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs.

(b) Past due loan amounts exclude PCI, even if contractually past due (or if we do not expect to collect principal or interest in full based on the original contractual terms), as we are currently accreting income over the remaining term of the loans.

(c) Net of unearned income, net deferred loan fees and costs, and unamortized discounts and premiums.

(d) Future accretable yield related to PCI loans is not included in the analysis of the loan portfolio.

Table of Contents

December 31, 2016 in millions	Current	30-59 Days Past Due (b)	60-89 Days Past Due (b)	90 and Greater Days Past Due (b)	Non-performing Loans	Total Past Due and Non-performing Loans	Purchased Credit Impaired	Total Loans (c), (d)
LOAN TYPE								
Commercial and industrial	$39,242	$ 58	$ 28	$ 31	$ 297	$ 414	112	$39,768
Commercial real estate:								
Commercial mortgage	14,655	93	9	6	26	134	322	15,111
Construction	2,314	—	—	2	3	5	26	2,345
Total commercial real estate loans	16,969	93	9	8	29	139	348	17,456
Commercial lease financing	4,641	28	3	5	8	44	—	4,685
Total commercial loans	$60,852	$ 179	$ 40	$ 44	$ 334	$ 597	460	$61,909
Real estate — residential mortgage	$5,098	$ 17	$ 5	$ 3	$ 56	$ 81	$ 368	$5,547
Home equity loans	12,327	49	29	16	223	317	30	12,674
Consumer direct loans	1,705	44	15	11	6	76	7	1,788
Credit cards	1,082	9	6	12	2	29	—	1,111
Consumer indirect loans	2,993	7	4	1	4	16	—	3,009
Total consumer loans	$23,205	$ 126	$ 59	$ 43	$ 291	$ 519	$ 405	$24,129
Total loans	$84,057	$ 305	$ 99	$ 87	$ 625	$ 1,116	$ 865	$86,038

(a) Amounts in table represent recorded investment and exclude loans held for sale. Recorded investment represents the face amount of the loan increased or decreased by applicable accrued interest, net deferred loan fees and costs, and unamortized premium or discount, and reflects direct charge-offs.

(b) Past due loan amounts exclude purchased impaired loans, even if contractually past due (or if we do not expect to collect principal or interest in full based on the original contractual terms), as we are currently accreting income over the remaining term of the loans.

(c) Net of unearned income, net deferred loan fees and costs, and unamortized discounts and premiums.

(d) Future accretable yield related to purchased credit impaired loans is not included in the analysis of the loan portfolio.

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

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

Commercial Credit Exposure — Excluding PCI
Credit Risk Profile by Creditworthiness Category (a), (b)

in millions	Commercial and industrial	RE — Commercial	RE — Construction	Commercial lease	Total

RATING	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016
Pass	$39,171	$ 37,845	$14,188	$ 14,308	$1,893	$ 2,287	$4,615	$ 4,632	$59,867	$ 59,072
Criticized (Accruing)	1,714	1,514	436	455	35	30	91	45	2,276	2,044
Criticized (Nonaccruing)	169	297	30	26	2	2	10	8	211	333
Total	$41,054	$ 39,656	$14,654	$ 14,789	$1,930	$ 2,319	$4,716	$ 4,685	$62,354	$ 61,449

(a) Credit quality indicators are updated on an ongoing basis and reflect credit quality information as of the dates indicated.

(b) The term criticized refers to those loans that are internally classified by Key as special mention or worse, which are asset quality categories defined by regulatory authorities. These assets have an elevated level of risk and may have a high probability of default or total loss. Pass rated refers to all loans not classified as criticized.

Table of Contents

Consumer Credit Exposure — Excluding PCI
Non-PCI Loans by Refreshed FICO Score [a]

in millions	Residential — Prime		Consumer direct loans		Credit cards		Consumer indirect loans		Total	
	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016
750 and above	$10,389	$ 9,818	$565	$ 498	$430	$ 453	$1,507	$ 1,266	$12,891	$ 12,035
660 to 749	5,278	5,266	688	661	492	525	1,191	1,195	7,649	7,647
Less than 660	1,551	1,617	213	194	123	132	473	543	2,360	2,486
No Score	110	1,122	318	428	—	1	27	5	455	1,556
Total	$17,328	$ 17,823	$1,784	$ 1,781	$1,045	$ 1,111	$3,198	$ 3,009	$23,355	$ 23,724

(a) Borrower FICO scores provide information about the credit quality of our consumer loan portfolio as they provide an indication as to the likelihood that a debtor will repay its debts. The scores are obtained from a nationally recognized consumer rating agency and are presented in the above table at the dates indicated.

Commercial Credit Exposure — PCI
Credit Risk Profile by Creditworthiness Category [a], [b]

in millions	Commercial and Industrial		RE — Commercial		RE — Construction		Commercial Lease		Total	
	September 30,	December 31,	September 30,	December 31,	September 30,	December 31,	September 30,	December 31,	September 30,	December 31,
RATING	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
Pass	$ 40	$ 12	$ 154	$ 139	$ 24	$ 21	—	—	$218	$ 172
Criticized	53	100	121	183	—	5	—	—	174	288
Total	$ 93	$ 112	$ 275	$ 322	$ 24	$ 26	—	—	$392	$ 460

(a) Credit quality indicators are updated on an ongoing basis and reflect credit quality information as of the dates indicated.

(b) The term “criticized” refers to those loans that are internally classified by Key as special mention or worse, which are asset quality categories defined by regulatory authorities. These assets have an elevated level of risk and may have a high probability of default or total loss. Pass rated refers to all loans not classified as criticized.

Consumer Credit Exposure — PCI
PCI Loans by Refreshed FICO Score [a]

in millions	Residential — Prime		Consumer direct loans		Credit cards		Consumer indirect loans		Total	
	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016
750 and above	$140	$ 133	1	—	—	—	—	—	$141	$ 133
660 to 749	131	127	$ 2	$ 2	—	—	—	—	133	129
Less than 660	111	133	2	4	—	—	—	—	113	137
No Score	4	5	—	1	—	—	—	—	4	6
Total	$386	$ 398	$ 5	$ 7	—	—	—	—	$391	$ 405

(a) Borrower FICO scores provide information about the credit quality of our consumer loan portfolio as they provide an indication as to the likelihood that a debtor will repay its debts. The scores are obtained from a nationally recognized consumer rating agency and are presented in the above table at the dates indicated.

We determine the appropriate level of the ALLL on at least a quarterly basis. The methodology for this determination is described in Note 1 (“Summary of Significant Accounting Policies”) under the heading “Allowance for Loan and Lease Losses” beginning on page 109 of our 2016 Form 10-K. We apply expected loss rates to existing loans with similar risk characteristics and exercise judgment to assess the impact of qualitative factors such as changes in economic conditions, changes in credit policies or underwriting standards, and changes in the level of credit risk associated with specific industries and markets.

For all commercial and consumer loan TDRs, regardless of size, as well as for impaired commercial loans with an outstanding balance of $2.5 million or greater, we conduct further analysis to determine the probable loss content and assign a specific allowance to the loan. We estimate the extent of the individual impairment for commercial loans and TDRs by comparing the recorded investment of the loan with the estimated present value of its future cash flows, the fair value of its underlying collateral, or the loan’s observable market price. Secured consumer loan TDRs that are discharged through Chapter 7 bankruptcy and not formally re-affirmed are adjusted to reflect the fair value of the underlying collateral, less costs to sell. Non-Chapter 7 consumer loan TDRs are evaluated at the account level and assigned a specific allocation based on the estimated present value of future cash flows using the loan’s effective interest rate. A specific allowance also may be assigned, even when sources of repayment appear sufficient, if we remain uncertain about whether the loan will be repaid in full. On at least a quarterly basis, we evaluate the appropriateness of our loss estimation methods to reduce differences between estimated incurred losses and actual losses.

Table of Contents

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

The ALLL on the acquired non-impaired loan portfolio is estimated using the same methodology as is used for the originated portfolio, however, the estimated ALLL is compared to the remaining accretable yield to determine if any incremental ALLL must be recorded. For PCI loans, Key estimates cash flows expected to be collected quarterly. Decreases in expected cash flows are recognized as impairment through a provision for credit losses and an increase in the ALLL. The ALLL at September 30, 2017, represents our best estimate of the probable credit losses inherent in the loan portfolio at that date.

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

	Three months ended September 30,		Nine months ended September 30,	
in millions	2017	2016	2017	2016
Balance at beginning of period — continuing operations	$870	$854	$858	$796
Charge-offs	(71)	(55)	(230)	(179)
Recoveries	39	11	74	46
Net loans and leases charged off	(32)	(44)	(156)	(133)
Provision for loan and lease losses from continuing operations	42	56	178	203
Foreign currency translation adjustment	—	(1)	—	(1)
Balance at end of period — continuing operations	$880	$865	$880	$865

The changes in the ALLL by loan category for the three and nine months ended September 30, 2017, and September 30, 2016, are as follows:

Three months ended September 30, 2017:

in millions	June 30, 2017	Provision	Charge-offs	Recoveries	September 30, 2017
Commercial and Industrial	$528	$ 8	$ (29)	$ 25	$ 532
Commercial real estate:					
Real estate — commercial mortgage	144	(1)	(6)	1	138
Real estate — construction	28	3	(2)	—	29
Total commercial real estate loans	172	2	(8)	1	167
Commercial lease financing	40	1	(1)	3	43
Total commercial loans	740	11	(38)	29	742
Real estate — residential mortgage	9	(2)	—	1	8
Home equity loans	42	(1)	(6)	4	39
Consumer direct loans	25	10	(8)	1	28
Credit cards	44	10	(11)	1	44

Consumer indirect loans	10	14		(8	) 3	19
Total consumer loans	130	31		(33	) 10	138
Total ALLL — continuing operations	870	42	(a)	(71	) 39	880
Discontinued operations	21	5		(10	) 2	18
Total ALLL — including discontinued operations	$ 891	$ 47		$ (81	) $ 41	$ 898

(a) Excludes a provision for losses on lending-related commitments of $9 million.

80

Three months ended September 30, 2016:

in millions	June 30, 2016	Provision	Charge-offs	Recoveries	September 30, 2016
Commercial and Industrial	$ 513	$ 19	$ (17)	$ 2	$ 517
Commercial real estate:					
Real estate — commercial mortgage	135	3	—	1	139
Real estate — construction	17	8	(9)	1	$ 17
Total commercial real estate loans	152	11	(9)	2	156
Commercial lease financing	45	5	(5)	—	45
Total commercial loans	710	35	(31)	4	718
Real estate — residential mortgage	18	(3)	(1)	1	15
Home equity loans	65	1	(5)	3	64
Consumer direct loans	19	4	(6)	1	18
Credit cards	30	17	(9)	1	39
Consumer indirect loans	12	1	(3)	1	11
Total consumer loans	144	20	(24)	7	147
Total ALLL — continuing operations	854	55 (a)	(55)	11	865
Discontinued operations	20	1	(6)	3	18
Total ALLL — including discontinued operations	$ 874	$ 56	$ (61)	$ 14	$ 883

(a) Includes a $1 million foreign currency translation adjustment. Excludes a provision for losses on lending-related commitments of $3 million.

Nine months ended September 30, 2017:

in millions	December 31, 2016	Provision	Charge-offs	Recoveries	September 30, 2017
Commercial and Industrial	$ 508	$ 93	$ (101)	$ 32	$ 532
Commercial real estate:					
Real estate — commercial mortgage	144	2	(9)	1	138
Real estate — construction	22	8	(2)	1	$ 29
Total commercial real estate loans	166	10	(11)	2	167
Commercial lease financing	42	5	(9)	5	43
Total commercial loans	716	108	(121)	39	742
Real estate — residential mortgage	17	(11)	(2)	4	8
Home equity loans	54	(4)	(23)	12	39
Consumer direct loans	24	26	(26)	4	28
Credit cards	38	36	(34)	4	44
Consumer indirect loans	9	23	(24)	11	19
Total consumer loans	142	70	(109)	35	138
Total ALLL — continuing operations	858	178 (a)	(230)	74	880
Discontinued operations	24	8	(20)	6	18
Total ALLL — including discontinued operations	$ 882	$ 186	$ (250)	$ 80	$ 898

(a) Excludes a provision for losses on lending-related commitments of $2 million.

Nine months ended September 30, 2016:

in millions	December 31, 2015	Provision	Charge-offs	Recoveries	September 30, 2016

Commercial and Industrial	$ 450	$ 137	$ (78)	$ 8	$ 517
Commercial real estate:					
Real estate — commercial mortgage	134	(1)	(3)	9	139
Real estate — construction	25	(1)	(9)	2	$ 17
Total commercial real estate loans	159	(2)	(12)	11	156
Commercial lease financing	47	7	(11)	2	45
Total commercial loans	656	142	(101)	21	718
Real estate — residential mortgage	18	(2)	(4)	3	15
Home equity loans	57	19	(22)	10	64
Consumer direct loans	20	12	(18)	4	18
Credit cards	32	29	(25)	3	39
Consumer indirect loans	13	2	(9)	5	11
Total consumer loans	140	60	(78)	25	147
Total ALLL — continuing operations	796	202 (a)	(179)	46	865
Discontinued operations	28	3	(21)	8	18
Total ALLL — including discontinued operations	$ 824	$ 205	$ (200)	$ 54	$ 883

(a) Includes a $1 million foreign currency translation adjustment. Excludes a credit for losses on lending-related commitments of $3 million.

Our allowance applies expected loss rates to our existing loans with similar risk characteristics as well as any adjustments to reflect our current assessment of qualitative factors, such as changes in economic conditions, underwriting standards, and concentrations of credit.

Table of Contents

There was $4 million of provision for loan and lease losses on PCI loans during the nine months ended September 30, 2017, and less than $1 million of provision for loan and lease losses on PCI loans during the three months ended September 30, 2017. There was $11 million of provision for loan and lease losses on PCI loans during the twelve months ended December 31, 2016. The provision for loan and lease losses on PCI loans was less than $1 million for the three and nine months ended September 30, 2016.

A breakdown of the individual and collective ALLL and the corresponding loan balances as of September 30, 2017, follows:

September 30, 2017	Allowance			Outstanding			
in millions	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Purchased Credit Impaired	Loans	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Purchased Credit Impaired
Commercial and industrial	$7	$ 522	3	$41,147	$ 157	$ 40,897	$ 93
Commercial real estate:							
Commercial mortgage	—	135	3	14,929	12	14,641	275
Construction	—	29	—	1,954	—	1,930	24
Total commercial real estate loans	—	164	3	16,883	12	16,571	299
Commercial lease financing	—	43	—	4,716	—	4,716	—
Total commercial loans	7	729	6	62,746	169	62,184	392
Real estate — residential mortgage	4	3	1	5,476	50	5,064	362
Home equity loans	7	31	1	12,238	117	12,098	24
Consumer direct loans	—	28	—	1,789	4	1,780	5
Credit cards	—	44	—	1,045	3	1,042	—
Consumer indirect loans	4	15	—	3,198	33	3,165	—
Total consumer loans	15	121	2	23,746	207	23,149	391
Total ALLL — continuing operations	22	850	8	86,492	376	85,333	783
Discontinued operations	4	14	—	1,372 (a)	26	1,346 (a)	—
Total ALLL — including discontinued operations	$26	$ 864	8	$87,864	$ 402	$ 86,679	$ 783

(a) Amount includes $2 million of loans carried at fair value that are excluded from ALLL consideration.

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

December 31, 2016	Allowance			Outstanding			
in millions	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Purchased Credit Impaired	Loans	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Purchased Credit Impaired
Commercial and Industrial	$17	$ 486	5	$39,768	$ 284	$ 39,372	$ 112
Commercial real estate:							
Commercial mortgage	—	144	—	15,111	5	14,784	322
Construction	—	22	—	2,345	—	2,319	26
Total commercial real estate loans	—	166	—	17,456	5	17,103	348
Commercial lease financing	—	42	—	4,685	—	4,685	—
Total commercial loans	17	694	5	61,909	289	61,160	460
Real estate — residential mortgage	2	15	—	5,547	51	5,128	368

Home equity loans	17	37	—	12,674	125	12,519	30
Consumer direct loans	—	24	—	1,788	3	1,778	7
Credit cards	—	38	—	1,111	3	1,108	—
Consumer indirect loans	1	8	—	3,009	30	2,979	—
Total consumer loans	20	122	—	24,129	212	23,512	405
Total ALLL — continuing operations	37	816	5	86,038	501	84,672	865
Discontinued operations	2	22	—	1,565 (a)	22	1,543 (a)	—
Total ALLL — including discontinued operations	$39	$ 838	$ 5	$87,603	$ 523	$ 86,215	$ 865

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

The liability for credit losses inherent in unfunded lending-related commitments, such as letters of credit and unfunded loan commitments, is included in “accrued expense and other liabilities” on the balance sheet. We establish the amount of this reserve by considering both historical trends and current market conditions quarterly, or more often if deemed necessary.

Table of Contents

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

in millions	Three months ended September 30, 2017	2016	Nine months ended September 30, 2017	2016
Balance at beginning of period	$ 48	$ 50	$ 55	$ 56
Provision (credit) for losses on lending-related commitments	9	3	2	(3)
Balance at end of period	$ 57	$ 53	$ 57	$ 53

Table of Contents

6. Fair Value Measurements

Fair Value Determination

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

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

- the amount of time since the last relevant valuation;
- whether there is an actual trade or relevant external quote available at the measurement date; and
- volatility associated with the primary pricing components.

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

- an independent review and approval of valuation models and assumptions;
- recurring detailed reviews of profit and loss; and
- a validation of valuation model components against benchmark data and similar products, where possible.

We recognize transfers between levels of the fair value hierarchy at the end of the reporting period. Quarterly, we review any changes to our valuation methodologies to ensure they are appropriate and justified, and refine our valuation methodologies if more market-based data becomes available. The Fair Value Committee, which is governed by ALCO, oversees the valuation process. Various working groups that report to the Fair Value Committee analyze and approve the underlying assumptions and valuation adjustments. Changes in valuation methodologies for Level 1 and Level 2 instruments are presented to the Accounting Policy group for approval. Changes in valuation methodologies for Level 3 instruments are presented to the Fair Value Committee for approval. The working groups are discussed in more detail in the qualitative disclosures within this note. Formal documentation of the fair valuation methodologies is prepared by the lines of business and support areas as appropriate. The documentation details the asset or liability class and related general ledger accounts, valuation techniques, fair value hierarchy level, market participants, accounting methods, valuation methodology, group responsible for valuations, and valuation inputs.

Additional information regarding our accounting policies for determining fair value is provided in Note 1 ("Summary of Significant Accounting Policies") under the heading "Fair Value Measurements" beginning on page 110 of our 2016 Form 10-K.

Qualitative Disclosures of Valuation Techniques

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

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

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

Table of Contents

- Securities are classified as Level 2 if quoted prices for identical securities are not available, and fair value is determined using pricing models (either by a third-party pricing service or internally) or quoted prices of similar securities. These instruments include municipal bonds, bonds backed by the U.S. government, corporate bonds, agency residential and CMBS, securities issued by the U.S. Treasury, money markets, and certain agency and corporate CMOs. Inputs to the pricing models include standard inputs (i.e. yields, benchmark securities, bids, and offers), actual trade data (i.e. spreads, credit ratings, and interest rates) for comparable assets, spread tables, matrices, high-grade scales, and option-adjusted spreads.
- Securities are classified as Level 3 when there is limited activity in the market for a particular instrument. To determine fair value in such cases, depending on the complexity of the valuations required, we use internal models based on certain assumptions or a third-party valuation service. At September 30, 2017, our Level 3 instruments consist of two convertible preferred securities. Our Corporate Strategy group is responsible for reviewing the valuation model and determining the fair value of these investments on a quarterly basis. The securities are valued using a cash flow analysis of the associated private company issuers. The valuations of the securities are negatively affected by projected net losses of the associated private companies and positively affected by projected net gains.

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

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

- review documentation received from our third-party pricing service regarding the inputs used in their valuations and determine a level assessment for each category of securities;
- substantiate actual inputs used for a sample of securities by comparing the actual inputs used by our third-party pricing service to comparable inputs for similar securities; and
- substantiate the fair values determined for a sample of securities by comparing the fair values provided by our third-party pricing service to prices from other independent sources for the same and similar securities. We analyze variances and conduct additional research with our third-party pricing service and take appropriate steps based on our findings.

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

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

Interest-bearing securities (i.e., loans) are valued on a quarterly basis. Valuation adjustments are determined by the Principal Investing Entities Deal Team and are subject to approval by the Investment Committee. Valuations of debt

Table of Contents

instruments are based on the Principal Investing Entities Deal Team's knowledge of the current financial status of the subject company, which is regularly monitored throughout the term of the investment. Significant, unobservable inputs used in the valuations of these investments include the company's payment history, adequacy of cash flows from operations, and current operating results, including market multiples and historical and forecast EBITDA. Inputs can also include the seniority of the debt, the nature of any pledged collateral, the extent to which the security interest is perfected, and the net liquidation value of collateral.

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

Our indirect investments include primary and secondary investments in private equity funds engaged mainly in venture- and growth-oriented investing. These investments do not have readily determinable fair values. Indirect investments are valued using a methodology that is consistent with accounting guidance allowing us to estimate fair value based upon net asset value per share (or its equivalent, such as member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed). On January 13, 2017, Key filed for an additional extension for illiquid funds, to retain certain indirect investments until the earlier of the date on which the investment is conformed or is expected to mature, or July 21, 2022. The application for an extension was approved on February 14, 2017. As of September 30, 2017, we have not committed to a plan to sell these investments. Therefore, these investments continue to be valued using the net asset value per share methodology.

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

The following table presents the fair value of our direct and indirect principal investments and related unfunded commitments at September 30, 2017, as well as financial support provided for the three and nine months ended September 30, 2017, and September 30, 2016.

			Financial support provided							
			Three months ended September 30,				Nine months ended September 30,			
	September 30, 2017		2017		2016		2017		2016	
in millions	Fair Value	Unfunded Commitments	Funded Commitments	Funded Other	Funded Commitments	Funded Other	Funded Commitments	Funded Other	Funded Commitments	Funded Other
INVESTMENT TYPE										
Direct investments [(a)]	$ 13	—	—		—	—	—	—	—	$ 13
Indirect investments [(b)] (measured at NAV)	138	$ 35	—		$ 2	—	$ 1	—	$ 5	—
Total	$ 151	$ 35	—		$ 2	—	$ 1	—	$ 5	$ 13

(a) Our direct investments consist of equity and debt investments directly in independent business enterprises. Operations of the business enterprises are handled by management of the portfolio company. The purpose of funding these enterprises is to provide financial support for business development and acquisition strategies. We infuse equity capital based on an initial contractual cash contribution and later from additional requests on behalf of the companies' management.

(b) Our indirect investments consist of buyout funds, venture capital funds, and fund of funds. These investments are generally not redeemable. Instead, distributions are received through the liquidation of the underlying investments of the fund. An investment in any one of these funds typically can be sold only with the approval of the fund's general partners. We estimate that the underlying investments of the funds will be liquidated over a period of one to eight years. The purpose of funding our capital commitments to these investments is to allow the funds to make additional follow-on investments and pay fund expenses until the fund dissolves. We, and all other investors in the fund, are obligated to fund the full amount of our respective capital commitments to the fund based on our and their respective ownership percentages, as noted in the applicable Limited Partnership Agreement.

Loans Held for Sale. As of August 1, 2016, we account for our residential mortgage loans held for sale at fair value on a recurring basis. The election of the fair value option aligns the accounting for the residential mortgages held for sale with the related forward mortgage loan sale commitments.

Residential mortgage loans are valued based on quoted market prices, where available, prices for other traded mortgage loans with similar characteristics, and purchase commitments and bid information received from market participants. The prices are adjusted as necessary to include the embedded servicing value in the loans and to take into consideration the specific characteristics of certain loans that are priced based on the pricing of similar loans. These adjustments represent unobservable inputs to the valuation but are not considered significant given the relative insensitivity of the value to changes in these inputs to the fair value of the loans. Accordingly, the majority of residential mortgage loans held for sale are classified as Level 2. Our residential mortgage activity also includes temporarily unsalable residential mortgage loans that are included in "Loans, net of unearned income" and loans with salability issues included in "Loans held for sale" on the balance sheet. These loans have an origination defect that makes them temporarily unable to be sold into the performing loan sales market. Because transaction details regarding sales of this type of loan are often unavailable, unobservable bid information from brokers and investors is heavily relied upon. Accordingly, based on the significance of unobservable inputs, these loans are classified as Level 3.

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

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

As a result of the First Niagara acquisition, we acquired First Niagara's residential mortgage business, which included interest rate lock commitments. These instruments are accounted for as a derivative and valued using models containing unobservable significant inputs. For valuation purposes, the loan amount associated with each interest rate lock commitment is adjusted by its modeled pull-through (an unobservable input) defined as the percentage of loans that will close prior to the expiration of the rate lock commitment, as adjusted for approved changes to the terms. Based on the significance of unobservable inputs, these instruments are classified as Level 3.

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

Table of Contents

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

Table of Contents

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Certain assets and liabilities are measured at fair value on a recurring basis in accordance with GAAP. The following tables present these assets and liabilities at September 30, 2017, and December 31, 2016.

September 30, 2017 in millions	Level 1	Level 2	Level 3	Total
ASSETS MEASURED ON A RECURRING BASIS				
Trading account assets:				
U.S. Treasury, agencies and corporations	—	$582	—	$582
States and political subdivisions	—	33	—	33
Collateralized mortgage obligations	—	—	—	—
Other mortgage-backed securities	—	124	—	124
Other securities	$ 2	35	—	37
Total trading account securities	2	774	—	776
Commercial loans	—	7	—	7
Total trading account assets	2	781	—	783
Securities available for sale:				
U.S. Treasury, agencies and corporations	—	158	—	158
States and political subdivisions	—	10	—	10
Agency residential collateralized mortgage obligations	—	15,401	—	15,401
Agency residential mortgage-backed securities	—	1,541	—	1,541
Agency commercial mortgage-backed securities	—	1,882	—	1,882
Other securities	—	—	$ 20	20
Total securities available for sale	—	18,992	20	19,012
Other investments:				
Principal investments:				
Direct	—	—	13	13
Indirect (measured at NAV) [a]	—	—	—	138
Total principal investments	—	—	13	151
Equity investments:				
Direct	—	2	—	2
Total equity investments	—	2	—	2
Total other investments	—	2	13	153
Loans, net of unearned income	—	—	—	—
Loans held for sale	—	58	2	60
Derivative assets:				
Interest rate	—	720	11	731
Foreign exchange	103	26	—	129
Commodity	—	144	—	144
Credit	—	—	1	1
Other	—	3	4	7
Derivative assets	103	893	16	1,012
Netting adjustments [b]	—	—	—	(390)
Total derivative assets	103	893	16	622
Accrued income and other assets	—	—	—	—
Total assets on a recurring basis at fair value	$ 105	$20,726	$ 51	$20,630
LIABILITIES MEASURED ON A RECURRING BASIS				
Bank notes and other short-term borrowings:				
Short positions	$ 89	$527	—	$616

Derivative liabilities:				
Interest rate	—	498	—	498
Foreign exchange	114	23	—	137
Commodity	—	135	—	135
Credit	—	6	—	6
Other	—	13	—	13
Derivative liabilities	114	675	—	789
Netting adjustments [b]	—	—	—	(557)
Total derivative liabilities	114	675	—	232
Accrued expense and other liabilities	—	—	—	—
Total liabilities on a recurring basis at fair value	$ 203	$1,202	—	$848

(a) Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheet.

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

89

Table of Contents

December 31, 2016 in millions	Level 1	Level 2	Level 3	Total
ASSETS MEASURED ON A RECURRING BASIS				
Trading account assets:				
U.S. Treasury, agencies and corporations	—	$655	—	$655
States and political subdivisions	—	8	—	8
Collateralized mortgage obligations	—	—	—	—
Other mortgage-backed securities	—	113	—	113
Other securities	—	73	—	73
Total trading account securities	—	849	—	849
Commercial loans	—	18	—	18
Total trading account assets	—	867	—	867
Securities available for sale:				
U.S. Treasury, agencies and corporations	—	184	—	184
States and political subdivisions	—	11	—	11
Agency residential collateralized mortgage obligations	—	16,408	—	16,408
Agency residential mortgage-backed securities	—	1,846	—	1,846
Agency commercial mortgage-backed securities	—	1,743	—	1,743
Other securities	$ 3	—	$ 17	20
Total securities available for sale	3	20,192	17	20,212
Other investments:				
Principal investments:				
Direct	—	—	27	27
Indirect (measured at NAV) [a]	—	—	—	158
Total principal investments	—	—	27	185
Equity and mezzanine investments:				
Indirect (measured at NAV) [a]	—	—	—	6
Total equity and mezzanine investments	—	—	—	6
Total other investments	—	—	27	191
Loans, net of unearned income	—	—	—	—
Loans held for sale	—	62	—	62
Derivative assets:				
Interest rate	—	923	7	930
Foreign exchange	114	9	—	123
Commodity	—	176	—	176
Credit	—	—	1	1
Other	—	2	2	4
Derivative assets	114	1,110	10	1,234
Netting adjustments [b]	—	—	—	(431)
Total derivative assets	114	1,110	10	803
Accrued income and other assets	—	8	—	8
Total assets on a recurring basis at fair value	$ 117	$22,239	$ 54	$22,143
LIABILITIES MEASURED ON A RECURRING BASIS				
Bank notes and other short-term borrowings:				
Short positions	$ 192	$616	—	$808
Derivative liabilities:				
Interest rate	—	737	—	737

Foreign exchange	102	11	—	113
Commodity	—	165	—	165
Credit	—	4	—	4
Other	—	1	—	1
Derivative liabilities	102	918	—	1,020
Netting adjustments [(b)]	—	—	—	(384)
Total derivative liabilities	102	918	—	636
Accrued expense and other liabilities	—	14	—	14
Total liabilities on a recurring basis at fair value	$ 294	$1,548	—	$1,458

(a) Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheet.

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

Table of Contents

Changes in Level 3 Fair Value Measurements

The following table shows the components of the change in the fair values of our Level 3 financial instruments for the three and nine months ended September 30, 2017, and September 30, 2016. We mitigate the credit risk, interest rate risk, and risk of loss related to many of these Level 3 instruments by using securities and derivative positions classified as Level 1 or Level 2. Level 1 and Level 2 instruments are not included in the following table. Therefore, the gains or losses shown do not include the impact of our risk management activities.

in millions	Beginning of Period Balance	Gains (Losses) Included in Other Comprehensive Income	Gains (Losses) Included in Earnings	Purchases	Sales	Settlements	Transfers Other	Transfers into Level 3 [a]	Transfers out of Level 3 [a]	End of Period Balance [f]	Unrealized Gains (Losses) Included in Earnings
Nine months ended September 30, 2017											
Securities available for sale											
Other securities	$ 17	$ 3	—	—	—	—	—	—	—	$ 20	—
Other investments											
Principal investments											
Direct	27	—	$ (7) [b]	—	$ (7)	—	—	—	—	13	$ (1) [b]
Derivative instruments [c]											
Interest rate	7	—	—	—	—	—	—	$ 13 [e]	$ (9) [e]	11	—
Credit	1	—	(12) [d]	—	—	$ 12	—	—	—	1	—
Other [g]	2	—	—	—	—	—	$ 2	—	—	4	—
Loans held for sale	—	—	—	—	(1)	—	3	—	—	2	—
Three months ended September 30, 2017											
Securities available for sale											
Other securities	$ 20	$ 1	—	—	—	—	—	—	$ (1)	$ 20	—
Other investments											
Principal investments											
Direct	15	—	$ (2) [b]	—	—	—	—	—	—	13	$ 2 [b]
Derivative instruments [c]											
Interest rate	16	—	—	—	—	—	—	$ 1 [e]	(6) [e]	11	—
Credit	1	—	(5) [d]	—	—	$ 5	—	—	—	1	—
Other [g]	4	—	—	—	—	—	—	—	—	4	—
Loans held for sale	—	—	—	—	$ (1)	—	$ 3	—	—	2	—

in millions	Beginning of Period Balance	Gains (Losses) Included in Earnings	Purchases	Sales	Settlements	Transfers Other	Transfers into Level 3 [a]	Transfers out of Level 3 [a]	End of Period Balance [f]	Unrealized Gains (Losses) Included in Earnings
Nine months ended September 30, 2016										
Securities available for sale										
Other securities	$ 17	—	—	—	—	—	—	—	$ 17	—
Other investments										
Principal investments										

Direct	50	$ 7 (b)	—	$(30)	—	—	—	—	27	$ 2 (b)
Other indirect	20	— (b)	—	(20)	—	—	—	—	—	(1) (b)
Derivative instruments (c)										
Interest rate	16	6 (d)	—	—	—	—	$ 8 (e)	$(21) (e)	9	—
Credit	1	(9) (d)	—	—	$ 10	—	—	—	2	—
Other (g)	—	—	$ 5	—	—	$ (1)	—	—	4	—
Three months ended September 30, 2016										
Securities available for sale										
Other securities	$ 17	—	—	—	—	—	—	—	$ 17	—
Other investments										
Principal investments										
Direct	24	$ 4 (b)	—	$(1)	—	—	—	—	27	$ 3 (b)
Derivative instruments (c)										
Interest rate	15	— (d)	—	—	—	—	$ 5 (e)	$(11) (e)	9	—
Credit	2	(3) (d)	—	—	$ 3	—	—	—	2	—
Other (g)	—	—	$ 5	—	—	$ (1)	—	—	4	—

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

(b) Realized and unrealized gains and losses on principal investments are reported in "net gains (losses) from principal investing" on the income statement.

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

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

(e) Certain derivatives previously classified as Level 2 were transferred to Level 3 because Level 3 unobservable inputs became significant. Certain derivatives previously classified as Level 3 were transferred to Level 2 because Level 3 unobservable inputs became less significant.

(f) There were no issuances for the nine-month periods ended September 30, 2017, and September 30, 2016.

(g) Amounts represent Level 3 interest rate lock commitments.

Table of Contents

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

Certain assets and liabilities are measured at fair value on a nonrecurring basis in accordance with GAAP. The adjustments to fair value generally result from the application of accounting guidance that requires assets and liabilities to be recorded at the lower of cost or fair value, or assessed for impairment. There were no liabilities measured at fair value on a nonrecurring basis at September 30, 2017, and December 31, 2016. The following table presents our assets measured at fair value on a nonrecurring basis at September 30, 2017, and December 31, 2016:

	September 30, 2017				December 31, 2016			
in millions	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
ASSETS MEASURED ON A NONRECURRING BASIS								
Impaired loans	—	—	$ 9	$ 9	—	—	$ 11	$ 11
Loans held for sale [(a)]	—	—	—	—	—	—	—	—
Accrued income and other assets	—	—	9	9	—	—	11	11
Total assets on a nonrecurring basis at fair value	—	—	$ 18	$ 18	—	—	$ 22	$ 22

(a) During the first nine months of 2017, we transferred $29 million of commercial loans and leases at their current fair value from held-for- sale status to the held-to-maturity portfolio, compared to $35 million during 2016.

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

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

Loans are evaluated for impairment on a quarterly basis. Loans included in the previous quarter's review are re-evaluated, and if their values have changed materially, the underlying information (loan balance and in most cases, collateral value) is compared. Material differences are evaluated for reasonableness, and the relationship managers and their senior managers consider these differences and determine if any adjustment is necessary. The inputs are developed and substantiated on a quarterly basis based on current borrower developments, market conditions, and collateral values. The following two internal methods are used to value impaired loans:

- Cash flow analysis considers internally developed inputs, such as discount rates, default rates, costs of foreclosure, and changes in collateral values.
- The fair value of the collateral, which may take the form of real estate or personal property, is based on internal estimates, field observations, and assessments provided by third-party appraisers. We perform or reaffirm appraisals of collateral-dependent impaired loans at least annually. Appraisals may occur more frequently if the most recent appraisal does not accurately reflect the current market, if the debtor is seriously delinquent or chronically past due, or there has been a material deterioration in the performance of the project or condition of the property. If an updated appraisal is less than the carrying amount of a collateral-dependent impaired loan, then the difference between the carrying amount and the updated appraisal value is reflected in the ALLL.

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

Commercial loans held for sale. Through a quarterly analysis of our loan portfolios held for sale, which include both performing and nonperforming commercial loans, we determine any adjustments necessary to record the portfolios at the lower of cost or fair value in accordance with GAAP. Our analysis concluded that there were no commercial loans held for sale adjusted to fair value at September 30, 2017, and December 31, 2016.

Market inputs, including updated collateral values, and reviews of each borrower's financial condition influence the inputs used in our internal models and other valuation methodologies. The valuations are prepared by the

Table of Contents

responsible relationship managers or analysts in our Asset Recovery Group and are reviewed and approved by the Asset Recovery Group Executive. Actual gains or losses realized on the sale of various commercial loans held for sale provide a back-testing mechanism for determining whether our valuations of these loans held for sale that are adjusted to fair value are appropriate.

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

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

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

Valuations of direct financing leases and operating lease assets held for sale are performed using an internal model that relies on market data, such as swap rates and bond ratings, as well as on our own assumptions about the exit market for the leases and details about the individual leases in the portfolio. The inputs based on our assumptions include changes in the value of leased items and internal credit ratings. These leases have been classified as Level 3 assets. KEF has master sale and assignment agreements with numerous institutional investors. Historically, multiple quotes are obtained, with the most reasonable formal quotes retained. These nonbinding quotes generally lead to a sale to one of the parties who provided the quote. Leases for which we receive a current nonbinding bid, and for which the sale is considered probable, may be classified as Level 2. The validity of these quotes is supported by historical and continued dealings with these institutions that have fulfilled the nonbinding quote in the past. In a distressed market where market data were not available, an estimate of the fair value of the leased asset may be used to value the lease, resulting in a Level 3 classification. In an inactive market, the market value of the assets held for sale is determined as the present value of the future cash flows discounted at the current buy rate. KEF Accounting calculates an estimated fair value buy rate based on the credit premium inherent in the relevant bond index and the appropriate swap rate on the measurement date. The amount of the adjustment is calculated as book value minus the present value of future cash flows discounted at the calculated buy rate.

Goodwill and other intangible assets. On a quarterly basis, we review impairment indicators to determine whether we need to evaluate the carrying amount of goodwill and other intangible assets assigned to Key Community Bank and Key Corporate Bank. We also perform an annual impairment test for goodwill. Accounting guidance permits an entity to first assess qualitative factors to determine whether additional goodwill impairment testing is required. We chose to utilize a qualitative assessment in our annual goodwill impairment testing performed during the fourth quarter of 2016. For additional information on the results of recent goodwill impairment testing, see Note 11 (“Goodwill and Other Intangible Assets”) beginning on page 166 of our 2016 Form 10-K.

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

Table of Contents

Our primary assumptions include attrition rates, alternative costs of funds, and rates paid on deposits. For additional information on the results of other intangible assets impairment testing, see Note 11 ("Goodwill and Other Intangible Assets") beginning on page 166 of our 2016 Form 10-K.

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

- Commercial Real Estate Valuation Process: When a loan is reclassified from loan status to OREO because we took possession of the collateral, the Asset Recovery Group Loan Officer, in consultation with our OREO group, obtains a broker price opinion or a third-party appraisal, which is used to establish the fair value of the underlying collateral. The determined fair value of the underlying collateral less estimated selling costs becomes the carrying value of the OREO asset. In addition to valuations from independent third-party sources, our OREO group also writes down the carrying balance of OREO assets once a bona fide offer is contractually accepted, where the accepted price is lower than the current balance of the particular OREO asset. The fair value of OREO property is re-evaluated every 90 days, and the OREO asset is adjusted as necessary.
- Residential Real Estate Valuation Process: The Asset Management team within our Risk Operations group is responsible for valuation policies and procedures of these loans. The current vendor partner provides monthly reporting of all broker price opinion evaluations, appraisals, and the monthly market plans. Market plans are reviewed monthly, and valuations are reviewed and tested monthly to ensure proper pricing has been established and guidelines are being met. Risk Operations Compliance validates and provides periodic testing of the valuation process. The Asset Management team reviews changes in fair value measurements. Third-party broker price opinions are reviewed every 180 days, and the fair value is written down based on changes to the valuation. External factors are documented and monitored as appropriate.

Quantitative Information about Level 3 Fair Value Measurements

The range and weighted average of the significant unobservable inputs used to fair value our material Level 3 recurring and nonrecurring assets at September 30, 2017, and December 31, 2016, along with the valuation techniques used, are shown in the following table:

September 30, 2017 dollars in millions	Fair Value of Level 3 Assets	Valuation Technique	Significant Unobservable Input	Range (Weighted Average)
Recurring				
Other investments — principal investments — direct:	$ 13	Individual analysis of the condition of each investment		
Debt instruments			EBITDA multiple	6.00 - 6.00 (6.00)
Nonrecurring				
Impaired loans	9	Fair value of underlying collateral	Discount	00.00 - 50.00% (23.00%)

December 31, 2016 dollars in millions	Fair Value of Level 3	Valuation Technique	Significant Unobservable Input	Range (Weighted-Average)

	Assets			
Recurring				
Other investments — principal investments — direct:	$ 27	Individual analysis of the condition of each investment		
Debt instruments			EBITDA multiple	6.30 - 7.00 (6.50)
Equity instruments of private companies			EBITDA multiple (where applicable)	N/A (6.3)
Nonrecurring				
Impaired loans	11	Fair value of underlying collateral	Discount	00.00 - 70.00% (46.00%)

94

Table of Contents

Fair Value Disclosures of Financial Instruments

The levels in the fair value hierarchy ascribed to our financial instruments and the related carrying amounts at September 30, 2017, and December 31, 2016, are shown in the following tables:

	September 30, 2017						
		Fair Value					
in millions	Carrying Amount	Level 1	Level 2	Level 3	Measured at NAV	Netting Adjustment	Total
ASSETS							
Cash and short-term investments [a]	$4,555	$4,555	—	—	—	—	$4,555
Trading account assets [b]	783	2	$781	—	—	—	783
Securities available for sale [b]	19,012	—	18,992	$ 20	—	—	19,012
Held-to-maturity securities [c]	10,276	—	10,109	—	—	—	10,109
Other investments [b]	728	—	2	584	138	—	724
Loans, net of allowance [d]	85,612	—	—	84,211	—	—	84,211
Loans held for sale [b]	1,341	—	58	1,283	—	—	1,341
Derivative assets [b]	622	103	893	16	—	(390) [f]	622
LIABILITIES							
Deposits with no stated maturity [a]	$92,207	—	$92,207	—	—	—	$92,207
Time deposits [e]	11,239	—	11,342	—	—	—	11,342
Short-term borrowings [a]	988	$89	899	—	—	—	988
Long-term debt [e]	15,100	13,752	1,741	—	—	—	15,493
Derivative liabilities [b]	232	114	675	—	—	(557) [f]	232

	December 31, 2016						
		Fair Value					
in millions	Carrying Amount	Level 1	Level 2	Level 3	Measured at NAV	Netting Adjustment	Total
ASSETS							
Cash and short-term investments [a]	$3,452	$3,452	—	—	—	—	$3,452
Trading account assets [b]	867	—	$867	—	—	—	867
Securities available for sale [b]	20,212	3	20,192	$ 17	—	—	20,212
Held-to-maturity securities [c]	10,232	—	10,007	—	—	—	10,007
Other investments [b]	738	—	—	569	$ 164	—	733
Loans, net of allowance [d]	85,180	—	—	83,285	—	—	83,285
Loans held for sale [b]	1,104	—	62	1,042	—	—	1,104
Derivative assets [b]	803	114	1,110	10	—	$ (431) [f]	803
LIABILITIES							
Deposits with no stated maturity [a]	$93,906	—	$93,906	—	—	—	$93,906
Time deposits [e]	10,181	—	10,267	—	—	—	10,267
Short-term borrowings [a]	2,310	$192	2,118	—	—	—	2,310
Long-term debt [e]	12,384	12,386	304	—	—	—	12,690
Derivative liabilities [b]	636	102	918	—	—	$ (384) [f]	636

Valuation Methods and Assumptions

(a) Fair value equals or approximates carrying amount. The fair value of deposits with no stated maturity does not take into consideration the value ascribed to core deposit intangibles.

(b) Information pertaining to our methodology for measuring the fair values of these assets and liabilities is included in the sections entitled “Qualitative Disclosures of Valuation Techniques” and “Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis” in this Note. Investments accounted for under the equity method are not included in this table. Investments accounted for under the cost method are classified as Level 3 assets. These investments are not actively traded in an open market as sales for these types of investments are rare. The carrying amount of the investments carried at cost are adjusted for declines in value if they are considered to be other-than-temporary. These adjustments are included in "other income" on the income statement.

(c) Fair values of held-to-maturity securities are determined by using models that are based on security-specific details, as well as relevant industry and economic factors. The most significant of these inputs are quoted market prices, interest rate spreads on relevant benchmark securities, and certain prepayment assumptions. We review the valuations derived from the models to ensure that they are reasonable and consistent with the values placed on similar securities traded in the secondary markets.

(d) The fair value of loans is based on the present value of the expected cash flows. The projected cash flows are based on the contractual terms of the loans, adjusted for prepayments and use of a discount rate based on the relative risk of the cash flows, taking into account the loan type, maturity of the loan, liquidity risk, servicing costs, and a required return on debt and capital. In addition, an incremental liquidity discount is applied to certain loans, using historical sales of loans during periods of similar economic conditions as a benchmark. The fair value of loans includes lease financing receivables at their aggregate carrying amount, which is equivalent to their fair value.

(e) Fair values of time deposits and long-term debt are based on discounted cash flows utilizing relevant market inputs.

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

Table of Contents

We use valuation methods based on exit market prices in accordance with applicable accounting guidance. We determine fair value based on assumptions pertaining to the factors that a market participant would consider in valuing the asset. A substantial portion of our fair value adjustments are related to liquidity. During 2016 and the first nine months of 2017, the fair values of our loan portfolios generally remained stable, primarily due to increasing liquidity in the loan markets. If we were to use different assumptions, the fair values shown in the preceding table could change. Also, because the applicable accounting guidance for financial instruments excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements, the fair value amounts shown in the table above do not, by themselves, represent the underlying value of our company as a whole.

Education lending business. The discontinued education lending business consists of loans in portfolio recorded at carrying value with appropriate valuation reserves, and loans in portfolio recorded at fair value. All of these loans were excluded from the table above as follows:

- Loans at carrying value, net of allowance, of $1.4 billion ($1.2 billion at fair value) at September 30, 2017, and $1.5 billion ($1.3 billion at fair value) at December 31, 2016;
- Portfolio loans at fair value of $2 million at September 30, 2017, and $3 million at December 31, 2016.

These loans and securities are classified as Level 3 because we rely on unobservable inputs when determining fair value since observable market data is not available.

Residential real estate mortgage loans. Residential real estate mortgage loans with carrying amounts of $5.5 billion at September 30, 2017, and $5.5 billion at December 31, 2016, are included in “Loans, net of allowance” in the previous table.

Short-term financial instruments. For financial instruments with a remaining average life to maturity of less than six months, carrying amounts were used as an approximation of fair values.

Table of Contents

7. Securities

Securities available for sale. These are securities that we intend to hold for an indefinite period of time but that may be sold in response to changes in interest rates, prepayment risk, liquidity needs, or other factors. Securities available for sale are reported at fair value. Realized gains and losses resulting from sales of securities using the specific identification method are included in “other income” on the income statement. Unrealized gains and losses (net of income taxes) deemed temporary are recorded in equity as a component of AOCI on the balance sheet. Unrealized losses on securities deemed to be “other-than-temporary” are included in “other income” on the income statement or in AOCI on the balance sheet in accordance with the applicable accounting guidance related to the recognition of OTTI of securities.

“Other securities” held in the available-for-sale portfolio consist primarily of convertible preferred stock issued by privately held companies.

Held-to-maturity securities. These are debt securities that we have the intent and ability to hold until maturity. Debt securities are carried at cost and adjusted for amortization of premiums and accretion of discounts using the interest method. This method produces a constant rate of return on the adjusted carrying amount.

“Other securities” held in the held-to-maturity portfolio consists primarily of foreign bonds.

The amortized cost, unrealized gains and losses, and approximate fair value of our securities available for sale and held-to-maturity securities are presented in the following tables. Gross unrealized gains and losses represent the difference between the amortized cost and the fair value of securities on the balance sheet as of the dates indicated. Accordingly, the amount of these gains and losses may change in the future as market conditions change.

	September 30, 2017			
in millions	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
SECURITIES AVAILABLE FOR SALE				
U.S. Treasury, agencies, and corporations	$160	—	$ 2	$158
States and political subdivisions	10	—	—	10
Agency residential collateralized mortgage obligations	15,580	$ 24	203	15,401
Agency residential mortgage-backed securities	1,547	4	10	1,541
Agency commercial mortgage-backed securities	1,928	—	46	1,882
Other securities	17	3	—	20
Total securities available for sale	$19,242	$ 31	$ 261	$19,012
HELD TO MATURITY SECURITIES				
Agency residential collateralized mortgage obligations	$7,788	$ 2	$ 143	$7,647
Agency residential mortgage-backed securities	601	1	2	600
Agency commercial mortgage-backed securities	1,872	8	33	1,847
Other securities	15	—	—	15
Total held-to-maturity securities	$10,276	$ 11	$ 178	$10,109

	December 31, 2016			
in millions	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
SECURITIES AVAILABLE FOR SALE				
U.S. Treasury, agencies, and corporations	$188	—	$ 4	$184

States and political subdivisions	11	—	—	11
Agency residential collateralized mortgage obligations	16,652	$ 31	275	16,408
Agency residential mortgage-backed securities	1,857	6	17	1,846
Agency commercial mortgage-backed securities	1,778	—	35	1,743
Other securities	21	—	1	20
Total securities available for sale	$20,507	$ 37	$ 332	$20,212
HELD TO MATURITY SECURITIES				
Agency residential collateralized mortgage obligations	$8,404	$ 1	$ 173	$8,232
Agency residential mortgage-backed securities	629	—	5	624
Agency commercial mortgage-backed securities	1,184	1	49	1,136
Other securities	15	—	—	15
Total held-to-maturity securities	$10,232	$ 2	$ 227	$10,007

Table of Contents

The following table summarizes our securities that were in an unrealized loss position as of September 30, 2017, and December 31, 2016.

	Duration of Unrealized Loss Position					
	Less than 12 Months		12 Months or Longer		Total	
in millions	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
September 30, 2017						
Securities available for sale:						
U.S Treasury, agencies, and corporations	$86	$ 1	$70	$ 1	$156	$ 2
Agency residential collateralized mortgage obligations	6,699	56	5,653	147	12,352	203
Agency residential mortgage-backed securities	1,245	9	88	1	1,333	10
Agency commercial mortgage-backed securities	760	11	1,122	35	1,882	46
Other securities (a)	2	—	—	—	2	—
Held-to-maturity:						
Agency residential collateralized mortgage obligations	3,208	52	3,778	91	6,986	143
Agency residential mortgage-backed securities	391	2	—	—	391	2
Agency commercial mortgage-backed securities	508	2	496	31	1,004	33
Other securities (b)	2	—	4	—	6	—
Total temporarily impaired securities	$12,901	$ 133	$11,211	$ 306	$24,112	$ 439
December 31, 2016						
Securities available for sale:						
U.S. Treasury, agencies, and corporations	$182	$ 4	—	—	$182	$ 4
Agency residential collateralized mortgage obligations	12,345	231	$1,410	$ 44	13,755	275
Agency residential mortgage-backed securities	1,452	17	—	—	1,452	17
Agency commercial mortgage-backed securities	1,482	35	—	—	1,482	35
Other securities (a)	2	—	3	1	5	1
Held-to-maturity:						
Agency residential collateralized mortgage obligations	7,028	156	518	17	7,546	173
Agency residential mortgage-backed securities	547	5	—	—	547	5
Agency commercial mortgage-backed securities	996	49	—	—	996	49
Other securities (b)	4	—	—	—	4	—
Total temporarily impaired securities	$24,038	$ 497	$1,931	$ 62	$25,969	$ 559

(a) Gross unrealized losses totaled less than $1 million for other securities available for sale at September 30, 2017, and December 31, 2016.

(b) Gross unrealized losses totaled less than $1 million for other securities held-to maturity at September 30, 2017 and December 31, 2016.

At September 30, 2017, we had $203 million of gross unrealized losses related to 352 fixed-rate agency residential CMOs that we invested in as part of our overall A/LM strategy. These securities had a weighted-average maturity of 4.12 years at September 30, 2017. We also had $10 million of gross unrealized losses related to 219 agency residential mortgage-backed securities positions, which had a weighted-average maturity of 3.93 years at September 30, 2017. Because these securities have a fixed interest rate, their fair value is sensitive to movements in market interest rates. These unrealized losses are considered temporary since we expect to collect all contractually due amounts from these securities. Accordingly, these investments were reduced to their fair value through OCI, not through earnings.

We regularly assess our securities portfolio for OTTI. The assessments are based on the nature of the securities, the underlying collateral, the financial condition of the issuer, the extent and duration of the loss, our intent related to the individual securities, and the likelihood that we will have to sell securities prior to expected recovery.

The debt securities identified as OTTI are written down to their current fair value. For those debt securities that we intend to sell, or more likely than not will be required to sell prior to the expected recovery of the amortized cost, the entire impairment (i.e., the difference between amortized cost and the fair value) is recognized in earnings. For those debt securities that we do not intend to sell, or more likely than not will not be required to sell prior to expected recovery, the credit portion of OTTI is recognized in earnings, while the remaining OTTI is recognized in equity as a component of AOCI on the balance sheet. As shown in the following table, we did not have any impairment losses recognized in earnings for the three and nine months ended September 30, 2017, and September 30, 2016.

Nine months ended September 30, 2017	
in millions	
Balance at December 31, 2016	$4
Impairment recognized in earnings	—
Balance at September 30, 2017	$4

Table of Contents

For the nine months ended September 30, 2017, net realized securities gains totaled less than $1 million.

At September 30, 2017, securities available for sale and held-to-maturity securities totaling $7.8 billion were pledged to secure securities sold under repurchase agreements, to secure public and trust deposits, to facilitate access to secured funding, and for other purposes required or permitted by law.

The following table shows our securities by remaining maturity. CMOs and other mortgage-backed securities (both of which are included in the securities available-for-sale portfolio) as well as the CMOs in the held-to-maturity portfolio are presented based on their expected average lives. The remaining securities, in both the available-for-sale and held-to-maturity portfolios, are presented based on their remaining contractual maturity. Actual maturities may differ from expected or contractual maturities since borrowers have the right to prepay obligations with or without prepayment penalties.

	Securities Available for Sale		Held to Maturity Securities	
September 30, 2017 in millions	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$190	$192	$76	$76
Due after one through five years	16,032	15,825	7,506	7,386
Due after five through ten years	3,010	2,985	2,087	2,054
Due after ten years	10	10	607	593
Total	$19,242	$19,012	$10,276	$10,109

Table of Contents

8. Derivatives and Hedging Activities

We are a party to various derivative instruments, mainly through our subsidiary, KeyBank. Derivative instruments are contracts between two or more parties that have a notional amount and an underlying variable, require a small or no net investment, and allow for the net settlement of positions. A derivative's notional amount serves as the basis for the payment provision of the contract and takes the form of units, such as shares or dollars. A derivative's underlying variable is a specified interest rate, security price, commodity price, foreign exchange rate, index, or other variable. The interaction between the notional amount and the underlying variable determines the number of units to be exchanged between the parties and influences the fair value of the derivative contract.

The primary derivatives that we use are interest rate swaps, caps, floors, and futures; foreign exchange contracts; commodity derivatives; and credit derivatives. Generally, these instruments help us manage exposure to interest rate risk, mitigate the credit risk inherent in our loan portfolio, hedge against changes in foreign currency exchange rates, and meet client financing and hedging needs. As further discussed in this note:

- interest rate risk is the risk that the EVE or net interest income will be adversely affected by fluctuations in interest rates;
- credit risk is the risk of loss arising from an obligor's inability or failure to meet contractual payment or performance terms; and
- foreign exchange risk is the risk that an exchange rate will adversely affect the fair value of a financial instrument.

Derivative assets and liabilities are recorded at fair value on the balance sheet, after taking into account the effects of bilateral collateral and master netting agreements. These agreements allow us to settle all derivative contracts held with a single counterparty on a net basis and to offset net derivative positions with related cash collateral, where applicable. As a result, we may have derivative contracts with negative fair values included in derivative assets on the balance sheet and contracts with positive fair values included in derivative liabilities.

At September 30, 2017, after taking into account the effects of bilateral collateral and master netting agreements, we had $24 million of derivative assets and $19 million of derivative liabilities that relate to contracts entered into for hedging purposes. As of the same date, after taking into account the effects of bilateral collateral and master netting agreements and a reserve for potential future losses, we had derivative assets of $598 million and derivative liabilities of $213 million that were not designated as hedging instruments.

Additional information regarding our accounting policies for derivatives is provided in Note 1 ("Summary of Significant Accounting Policies") under the heading "Derivatives" beginning on page 112 of our 2016 Form 10-K.

Derivatives Designated in Hedge Relationships

Net interest income and the EVE change in response to changes in the mix of assets, liabilities, and off-balance sheet instruments and the associated interest rates tied to each instrument. In addition, differences in the repricing and maturity characteristics of interest-earning assets and interest-bearing liabilities cause net interest income and the EVE to fluctuate. We utilize derivatives that have been designated as part of a hedge relationship in accordance with the applicable accounting guidance to manage net interest income and EVE to within our stated risk tolerances. The primary derivative instruments used to manage interest rate risk are interest rate swaps, which convert the contractual interest rate index of agreed-upon amounts of assets and liabilities (i.e., notional amounts) to another interest rate index.

We designate certain "receive fixed/pay variable" interest rate swaps as fair value hedges. These contracts convert certain fixed-rate long-term debt into variable-rate obligations, thereby modifying our exposure to changes in interest rates. As a result, we receive fixed-rate interest payments in exchange for making variable-rate payments over the lives of the contracts without exchanging the notional amounts.

Similarly, we designate certain “receive fixed/pay variable” interest rate swaps as cash flow hedges. These contracts effectively convert certain floating-rate loans into fixed-rate loans to reduce the potential adverse effect of interest rate decreases on future interest income. Again, we receive fixed-rate interest payments in exchange for making variable-rate payments over the lives of the contracts without exchanging the notional amounts.

Table of Contents

We also designate certain “pay fixed/receive variable” interest rate swaps as cash flow hedges. These swaps convert certain floating-rate debt into fixed-rate debt. We also use these swaps to manage the interest rate risk associated with anticipated sales of certain commercial real estate loans. The swaps protect against the possible short-term decline in the value of the loans that could result from changes in interest rates between the time they are originated and the time they are sold.

We use foreign currency forward transactions to hedge the foreign currency exposure of our net investment in various foreign equipment finance entities. These entities are denominated in a non-U.S. currency. These swaps are designated as net investment hedges to mitigate the exposure of measuring the net investment at the spot foreign exchange rate.

Derivatives Not Designated in Hedge Relationships

On occasion, we enter into interest rate swap contracts to manage economic risks but do not designate the instruments in hedge relationships. Excluding contracts addressing customer exposures, the amount of derivatives hedging risks on an economic basis at September 30, 2017, was not significant.

Like other financial services institutions, we originate loans and extend credit, both of which expose us to credit risk. We actively manage our overall loan portfolio and the associated credit risk in a manner consistent with asset quality objectives and concentration risk tolerances to mitigate portfolio credit risk. Purchasing credit default swaps enables us to transfer to a third party a portion of the credit risk associated with a particular extension of credit, including situations where there is a forecast sale of loans. Beginning in the first quarter of 2014, we began purchasing credit default swaps to reduce the credit risk associated with the debt securities held in our trading portfolio. We may also sell credit derivatives to offset our purchased credit default swap position prior to maturity. Although we use credit default swaps for risk management purposes, they are not treated as hedging instruments.

We also enter into derivative contracts for other purposes, including:

- interest rate swap, cap, and floor contracts generally entered into to accommodate the needs of commercial loan clients;
- energy and base metal swap and option contracts entered into to accommodate the needs of clients;
- foreign exchange forward and option contracts entered into primarily to accommodate the needs of clients; and
- futures contracts and positions with third parties that are intended to offset or mitigate the interest rate or market risk related to client positions discussed above.

These contracts are not designated as part of hedge relationships.

Fair Values, Volume of Activity, and Gain/Loss Information Related to Derivative Instruments

The following table summarizes the fair values of our derivative instruments on a gross and net basis as of September 30, 2017, and December 31, 2016. The change in the notional amounts of these derivatives by type from December 31, 2016, to September 30, 2017, indicates the volume of our derivative transaction activity during the first nine months of 2017. The notional amounts are not affected by bilateral collateral and master netting agreements. The derivative asset and liability balances are presented on a gross basis, prior to the application of bilateral collateral and master netting agreements. Total derivative assets and liabilities are adjusted to take into account the impact of legally enforceable master netting agreements that allow us to settle all derivative contracts with a single counterparty on a net basis and to offset the net derivative position with the related cash collateral. Where master netting agreements are not in effect or are not enforceable under bankruptcy laws, we do not adjust those derivative assets and liabilities with counterparties. Securities collateral related to legally enforceable master netting agreements is not offset on the balance sheet. Our derivative instruments are included in “derivative assets” or “derivative liabilities” on the balance sheet, as indicated in the following table:

Table of Contents

	September 30, 2017			December 31, 2016		
		Fair Value			Fair Value	
in millions	Notional Amount	Derivative Assets	Derivative Liabilities	Notional Amount	Derivative Assets	Derivative Liabilities
Derivatives designated as hedging instruments:						
Interest rate	$25,489	$ 87	$ 29	$24,237	$ 189	$ 94
Foreign exchange	290	—	15	282	6	4
Total	25,779	87	44	24,519	195	98
Derivatives not designated as hedging instruments:						
Interest rate	60,887	644	469	55,315	741	643
Foreign exchange	8,664	129	122	6,230	117	109
Commodity	1,696	144	135	1,474	176	165
Credit	484	1	6	360	1	4
Other [a]	2,359	7	13	390	4	1