Discover Financial Services
Form 10-K
February 25, 2015

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K
(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the calendar year ended December 31, 2014

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number 001-33378

DISCOVER FINANCIAL SERVICES
(Exact name of registrant as specified in its charter)

Delaware	36-2517428
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2500 Lake Cook Road, Riverwoods, Illinois 60015	(224) 405-0900
(Address of principal executive offices, including zip code)	(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, par value $0.01 per share	New York Stock Exchange
Depositary Shares, each representing 1/40th interest in a share of Fixed Rate Non-Cumulative Perpetual Preferred Stock, Series B, par value $0.01 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No x

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

Large accelerated filer x Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company) Smaller reporting company o
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No x
The aggregate market value of the common equity held by non-affiliates of the registrant on the last business day of the registrant's most recently
completed second fiscal quarter was approximately $28,651,886,813.
As of February 20, 2015, there were 447,239,938 shares of the registrant's Common Stock, par value $0.01 per share, outstanding.
DOCUMENTS INCORPORATED BY REFERENCE
Portions of the registrant's definitive proxy statement for its annual stockholders' meeting to be held on April 29, 2015 are incorporated by reference in Part III of this Form 10-K.

DISCOVER FINANCIAL SERVICES
Annual Report on Form 10-K for the calendar year ended December 31, 2014

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Except as otherwise indicated or unless the context otherwise requires, “Discover Financial Services,” “Discover,” “DFS,” “we,” “us,” “our,” and “the Company” refer to Discover Financial Services and its subsidiaries.
We own or have rights to use the trademarks, trade names and service marks that we use in conjunction with the operation of our business, including, but not limited to: Discover®, PULSE®, Cashback Bonus®, Discover Cashback Checking®, Discover® More® Card, Discover it®, Discover® Motiva℠ Card, Discover® Open Road® Card, Discover® Network and Diners Club International®. All other trademarks, trade names and service marks included in this annual report on Form 10-K are the property of their respective owners.

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Part I.

Item 1. Business

Introduction

Discover Financial Services is a direct banking and payment services company. We were incorporated in Delaware in 1960. We are a bank holding company under the Bank Holding Company Act of 1956 as well as a financial holding company under the Gramm-Leach-Bliley Act and therefore are subject to oversight, regulation and examination by the Board of Governors of the Federal Reserve System (the “Federal Reserve”). We provide direct banking products and services and payment services through our subsidiaries. We offer our customers credit card loans, private student loans, personal loans, home loans, home equity loans and deposit products. We had $70.0 billion in loan receivables and $28.8 billion in deposits issued through direct-to-consumer channels and affinity relationships at December 31, 2014. We operate the Discover Network, the PULSE network (“PULSE”), and Diners Club International (“Diners Club”). The Discover Network processes transactions for Discover-branded credit cards and provides payment transaction processing and settlement services. PULSE operates an electronic funds transfer network, providing financial institutions issuing debit cards on the PULSE network with access to ATMs domestically and internationally, as well as point-of-sale ("POS") terminals at retail locations throughout the U.S. for debit card transactions. Diners Club is a global payments network of licensees, which are generally financial institutions, that issue Diners Club branded charge cards and/or provide card acceptance services.

In December 2012, our board of directors approved a change in our fiscal year end from November 30 to December 31 of each year. This fiscal year change was effective January 1, 2013. As a result of the change, we had a one month transition period in December 2012. The audited results for the one month ended December 31, 2012 are included in this report.

Available Information

We make available, free of charge through the investor relations page of our internet site www.discover.com, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, Forms 3, 4 and 5 filed by or on behalf of directors and executive officers, and any amendments to those documents filed with or furnished to the Securities and Exchange Commission (the "SEC") pursuant to the Securities Exchange Act of 1934. These filings are available as soon as reasonably practicable after they are filed with or furnished to the SEC. In addition, the following information is available on the investor relations page of our internet site: (i) our Corporate Governance Policies; (ii) our Code of Ethics and Business Conduct; and (iii) the charters of the Audit, Compensation and Leadership Development, Nominating and Governance, and Risk Oversight Committees of our board of directors. These documents are also available in print without charge to any person who requests them by writing or telephoning our principal executive offices: Discover Financial Services, Office of the Corporate Secretary, 2500 Lake Cook Road, Riverwoods, Illinois 60015, U.S.A., telephone number (224) 405-0900.

Operating Model

We manage our business activities in two segments: Direct Banking and Payment Services. Our Direct Banking segment includes consumer banking and lending products, specifically Discover-branded credit cards issued to individuals on the Discover Network and other consumer banking products and services, including private student loans, personal loans, home loans, home equity loans, prepaid cards and other consumer lending and deposit products. Our Payment Services segment includes PULSE, Diners Club and our Network Partners business, which provides payment transaction processing and settlement services on the Discover Network.

We are principally engaged in providing products and services to customers in the United States, although the royalty and licensee revenue we receive from Diners Club licensees is mainly derived from sources outside of the United States. For quantitative information concerning our geographic distribution, see Note 4: Loan Receivables to our consolidated financial statements.

Below are descriptions of the principal products and services of each of our reportable segments. For additional financial information relating to our business and our operating segments, see Note 22: Segment Disclosures to our consolidated financial statements.

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Direct Banking

Set forth below are descriptions of our credit cards, student loans, personal loans, home loans, home equity loans and deposit products. For additional information regarding the terms and conditions of these products, see "— Product Terms and Conditions."

Credit Cards

We currently offer credit cards issued to consumers. Our credit card customers are permitted to "revolve" their balances and repay their obligations over a period of time and at an interest rate set forth in their cardmember agreements, which may be either fixed or variable. The interest that we earn on revolving credit card balances makes up approximately 84% of our total interest income. We also charge customers other fees as specified in the cardmember agreements. These fees may include fees for late payments, balance transfer transactions and cash advance transactions.

Our credit card customers' transactions in the U.S. are processed over the Discover Network. Where we have a direct relationship with a merchant, which is the case with respect to our large merchants representing a majority of Discover card sales volume, we receive discount and fee revenue from merchants. Discount and fee revenue is based on pricing that is set forth in contractual agreements with each such merchant and is based on a number of factors including industry practices, special marketing arrangements, competitive pricing levels and merchant size. Where we do not have a direct relationship with a merchant, we receive acquirer interchange and assessment fees from the merchant acquirer that settles transactions with the merchant. The amount of this fee is based on a standardized schedule and can vary based on the type of merchant.

Most of our cards offer the Cashback Bonus rewards program, the costs of which we record as a reduction of discount and interchange revenue. See "— Marketing — Rewards/Cashback Bonus" for further discussion of our programs offered.

The following chart* shows the Discover card transaction cycle as processed on the Discover Network:

Student Loans

Our private student loans are available to students attending eligible non-profit four-year undergraduate and graduate schools. We also offer certain post-graduate loans, including bar study and residency loans. We encourage students to borrow responsibly and maximize grants, scholarships and other free financial aid before taking student loans.

We currently offer fixed and variable rate private student loans originated by Discover Bank. We market our student loans online and through direct mail and email to existing and potential customers. We also work with school financial aid offices to create awareness of our products with students. Students can apply for our student loans online,

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by phone, or by mail, and we have dedicated staff within our call centers to service student loans. We invite applicants to apply with a creditworthy cosigner, which may improve the likelihood for loan approval and a lower interest rate. As part of the loan approval process, all of our student loans, except for bar study and residency loans, are certified and disbursed through the school to ensure students do not borrow more than the cost of attendance less other financial aid. Upon graduation, for variable loans originated before May 2014, students are generally eligible to receive a graduation reward. Students may redeem their graduation reward as a credit to the balance of any of their Discover student loans or as a direct deposit to a bank account. For all loans originated in May 2014 and after, students are generally eligible to receive a reward for achieving a specified grade point average during the academic period covered by the loan.

Personal Loans

Our personal loans are unsecured loans with fixed interest rates, terms and payments. These loans are primarily intended to help customers consolidate existing debt, although they can be used for other reasons. We generally market personal loans to our existing credit card customers through direct mail, statement inserts and email. We also market personal loans to non-Discover customers through direct mail. Customers can submit applications via phone, online or through the mail, and can service their accounts online or by phone.

Home Loans and Home Equity Loans

In 2012, we began offering home mortgage loans and related services to help consumers finance home purchases and refinance existing home mortgages. We offer prime adjustable, fixed-rate conforming, jumbo, Federal Housing Administration ("FHA") and U.S. Department of Veterans Affairs (“VA”) first lien loans to qualified applicants. We generally market home loans to existing Discover customers through direct mail, email, statement envelopes and inserts, and advertising on Discover websites. We also market home loans to non-Discover customers through direct mail, internet advertising, including search engine marketing, display banners, internet lead aggregators, rate tables on financial websites and social media. Consumers can apply for or obtain information about home loans by mail or online, or they can speak directly to a dedicated mortgage banker over the phone. Loans are funded and closed using proceeds principally from borrowings under a third-party warehouse line of credit. Substantially all funded loans and the related loan servicing rights are sold to investors in the secondary market, generally within 30 days of funding. The proceeds from such sales are used to repay borrowings under the warehouse line of credit. In addition to funding loans, we offer escrow and title services to home loan customers. For more information regarding our warehouse line of credit, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Funding Sources — Short-Term Borrowings."

We offer closed-end home equity loans to help consumers improve their homes as well as payoff higher interest debt. These loans are fixed term and rate loans that provide consumers the stability of a fixed payment on their obligation while being secured against the equity in their homes. We market this product primarily to existing card customers through a mix of direct mail, internet advertising and email. Non-Discover customers can obtain information regarding Discover home equity products on our website and have the ability to apply by calling a personal banker.

Deposits

We obtain deposits from consumers directly or through affinity relationships ("direct-to-consumer deposits") and through third-party securities brokerage firms that offer our deposits to their customers ("brokered deposits"). Our deposit products include certificates of deposit, money market accounts, savings accounts, checking accounts and Individual Retirement Arrangement ("IRA") certificates of deposit. We market our direct-to-consumer deposit products to our existing customer base and other prospective customers through the use of our website, mobile platform, print materials, affinity arrangements with third parties and internet advertising. Customers can apply for, fund, and service their deposit accounts online or via phone, where we have a dedicated U.S. based staff within our call centers to service deposit accounts. For more information regarding our deposit products, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Funding Sources — Deposits."

Payment Services

Set forth below are descriptions of PULSE, Diners Club and our Network Partners business, which provides payment transaction processing and settlement services on the Discover Network.

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PULSE Network

Our PULSE network is one of the nation’s leading debit/ATM networks. PULSE links cardholders of more than 7,200 financial institutions with ATMs and POS terminals located throughout the United States. This includes more than 3,700 financial institutions with which PULSE has direct relationships and approximately 3,400 additional financial institutions through agreements PULSE has with other debit networks. PULSE also provides cash access at 1.6 million ATMs in 130 countries.

PULSE's primary source of revenue is transaction fees charged for switching and settling ATM, personal identification number ("PIN") POS debit and signature debit transactions initiated through the use of debit cards issued by participating financial institutions. In addition, PULSE offers a variety of optional products and services that produce income for the network, including signature debit transaction processing, debit card fraud detection and risk mitigation services, and connections to other regional and national electronic funds transfer networks.

When a financial institution joins the PULSE network, debit cards issued by that institution are eligible to be used at all of the ATMs and PIN POS debit terminals that participate in the PULSE network, and the PULSE mark can be used on that institution's debit cards and ATMs. In addition, financial institution participants may sponsor merchants, direct processors and independent sales organizations to participate in the PULSE PIN POS and ATM debit service. A participating financial institution assumes liability for transactions initiated through the use of debit cards issued by that institution, as well as for ensuring compliance with PULSE's operating rules and policies applicable to that institution's debit cards, ATMs and, if applicable, sponsored merchants, direct processors and independent sales organizations.

When PULSE enters into a network-to-network agreement with another debit network, the other network's participating financial institutions' debit cards can be used at terminals in the PULSE network. PULSE does not have a direct relationship with these financial institutions and the other network bears the financial responsibility for transactions of those financial institutions' cardholders and for ensuring compliance with PULSE's operating rules.

Diners Club

Our Diners Club business maintains an acceptance network in over 185 countries and territories through its relationships with over 80 licensees, which are generally financial institutions. We generally do not directly issue Diners Club cards to consumers, but grant our licensees the right to issue Diners Club branded cards and/or provide card acceptance services. Our licensees pay us royalties for the right to use the Diners Club brand, which is our primary source of Diners Club revenues. We also earn revenue from providing various support services to our Diners Club licensees, including processing and settlement of cross border transactions. We also provide a centralized service center and internet services to our licensees.

When Diners Club cardholders use their cards outside the host country or territory of the issuing licensee, transactions are routed and settled over the Diners Club network through its centralized service center. In order to increase merchant acceptance in certain targeted countries and territories, we work with merchant acquirers to offer Diners Club and Discover acceptance to their merchants. These acquirers are granted licenses to market the Diners Club brands to existing and new merchants. As we continue to work toward achieving full card acceptance across our networks, Discover customers are using their cards at an increasing number of merchant and ATM locations that accept Diners Club cards around the world. Diners Club cardholders with cards issued by licensees outside of North America continue to use their cards on the Discover Network in North America and on the PULSE and Diners Club network domestically and internationally.

Network Partners Business

We have agreements with a number of financial institutions, networks and commercial service providers for issuance of products or processing of payments on Discover networks. We refer to these financial institutions, networks and commercial service providers as "Network Partners." We may earn merchant discount and acquirer assessments net of issuer fees paid, in addition to other fees, for processing transactions for Network Partners.

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The following chart* shows an example of Network Partners transaction cycle:

* * *

The discussion below provides additional detail concerning the supporting functions of our two segments. The credit card, student loan, personal loan, home loan, home equity loan and deposit products issued through our Direct Banking segment require significant consumer portfolio investments in risk management, marketing, customer service and related technology, whereas the operation of our Payment Services business requires that we invest in the technology to manage risk and service network partners, merchants and merchant acquirer relationships.

Credit Risk Management

Credit risk management is a critical component of our management and growth strategy. Credit risk refers to the risk of loss arising from borrower default when borrowers are unable or unwilling to meet their financial obligations to us. Our credit risk arising from consumer lending products is generally highly diversified across millions of accounts without significant individual exposures. We manage credit risk primarily based on customer segments and product types. See "— Risk Management" for more information regarding how we define and manage our credit and other risks.

Account Acquisition (New Customers)

We acquire new credit card customers through direct mail, internet, media advertising, merchant or partner relationships, or through unsolicited individual applications. We also acquire new student loan, personal loan and home loan customers through similar channels. In all cases we have a rigorous process for screening applicants.

To identify credit-worthy prospective customers, our credit risk management and marketing teams use proprietary analytical tools to match our product offerings with customer’s needs. We consider the prospective customer's financial stability, as well as ability and willingness to pay.

We assess the creditworthiness of each consumer loan applicant through evaluating applicant’s credit information provided by credit bureaus and information from other sources. The assessment is performed using our credit scoring systems, both externally developed and proprietary. For our unsecured lending products, we also use experienced credit underwriters to supplement our automated decision-making processes. For our home loan and home equity products, experienced credit underwriters must review and approve each application.

Upon approval of a customer's application for one of our unsecured lending and home equity products, we assign a specific annual percentage rate using an analytically driven pricing framework that simultaneously provides competitive pricing for customers and seeks to maximize revenue on a risk-adjusted basis. For our credit card loans, we also assign a credit line based on risk level and expected return.

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Portfolio Management (Existing Customers)

The revolving nature of our credit card loans requires that we regularly assess the credit risk exposure of such accounts. This assessment uses the individual's Discover account performance information as well as information from credit bureaus. We utilize statistical evaluation models to support the measurement and management of credit risk. At the individual customer level, we use custom risk models together with generic industry models as an integral part of the credit decision-making process. Depending on the duration of the customer's account, risk profile and other performance metrics, the account may be subject to a range of account management treatments, including transaction authorization limits and increases or decreases on credit limits. Our installment loans are billed according to an amortization schedule that is calculated at the time of the disbursement of the loan and, in the case of deferred student loans, at the time the loan enters repayment.

Customer Assistance

We provide our customers with a variety of tools to proactively manage their accounts, including electronic payment reminders and a website dedicated to customer education, as further discussed under the heading "— Customer Service." These tools are designed to limit a customer's risk of becoming delinquent. When a customer's account becomes delinquent or is at risk of becoming delinquent, we employ a variety of strategies to assist customers in becoming current on their accounts.

All monthly billing statements of accounts with past due amounts include a request for payment of such amounts. Customer assistance personnel generally initiate contact with customers within 30 days after any portion of their balance becomes past due. The nature and the timing of the initial contact, typically a personal call or letter, are determined by a review of the customer's prior account activity and payment habits.

We reevaluate our collection efforts, and consider the implementation of other techniques, as a customer becomes increasingly delinquent. We limit our exposure to delinquencies through controls within our process for authorizing transactions and credit limits and criteria-based account suspension and revocation. In situations involving customers with financial difficulties, we may enter into arrangements to extend or otherwise change payment schedules, lower interest rates and/or waive fees to aid customers in becoming current on their obligations to us. For more information see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Loan Quality — Modified and Restructured Loans."

Marketing

In addition to working with our credit risk management personnel on account acquisition and portfolio management, our marketing group provides other key functions, including product development, management of our Cashback Bonus and other rewards programs, protection product management, and brand and advertising management.

Product Development

In order to attract and retain customers and merchants, we continue to develop new programs, features, and benefits and market them through a variety of channels, including mail, phone and online. Targeted marketing efforts may include balance transfer offers and reinforcement of our Cashback Bonus and other rewards programs. Through the development of a large prospect database, use of credit bureau data and use of a customer contact strategy and management system, we have been able to improve our modeling and customer engagement capabilities, which helps optimize product, pricing and channel selection.

Rewards / Cashback Bonus

Our cardmembers use several card products that allow them to earn their rewards based on how they want to use credit, as set forth below.

- Discover it card offers 5% Cashback Bonus in categories that change throughout the year up to a quarterly maximum (signing up is required) and 1% Cashback Bonus on all other purchases, as well as other benefits.
- The newly launched Discover it Miles card offers 1.5 miles for every dollar spent on purchases, no annual fee and an annual credit of up to $30 for in-flight Wi-Fi charges.
- Discover it Chrome card offers 2% Cashback Bonus on gas and restaurants up to a quarterly maximum (no sign up required) and 1% Cashback Bonus on all other purchases as well as other benefits.

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- Discover More card offers 5% Cashback Bonus in categories that change throughout the year up to a quarterly maximum (signing up is required) and up to 1% Cashback Bonus* on all other purchases.
- Discover Open Road card offers 2% Cashback Bonus on the first $250 spent in combined gas and restaurant purchases each billing period and up to 1% Cashback Bonus* on all other purchases.
- Miles by Discover customers receive two miles for every $1 on the first $3,000 spent in travel and restaurant purchases each year, one mile for every $1 spent thereafter, and one mile for every $1 spent on all other purchases.
- Escape by Discover customers receive two miles for every $1 on all purchases. This card has a $60 annual fee.
- Discover Business card offers 5% Cashback Bonus on the first $2,000 spent in office supply purchases, 2% Cashback Bonus on the first $2,000 spent in gas purchases each year and up to 1% Cashback Bonus* on all other purchases.

* With Discover Deals, customers can shop at top merchants and earn additional Cashback Bonus or miles, a statement credit on their Discover account or instant savings at checkout both online and in stores. Cashback Bonus can be redeemed for (i) merchant partner gift cards (starting at $20) that add $5 or more to their reward, (ii) Discover gift cards (starting at $20, available through April 1, 2015), (iii) charitable donations to select charities (starting at 1 cent), (iv) in the form of a statement credit (starting at 1 cent), or (v) electronic deposit to a bank account (starting at 1 cent). Miles can be redeemed for (i) partner gift cards (starting at 1,000 miles), (ii) Discover gift cards (starting at 5,000 miles, available through April 1, 2015), (iii) cash in the form of statement credits or direct deposits (starting at 2 miles), (iv) charitable donations to select charities (starting at 2 miles), or (v) for the Escape card only, travel credits starting at 10,000 miles.

Protection Products

We currently service and maintain existing enrollments of the protection products detailed below for our credit card customers. Although we suspended new sales of these products to consumers at the end of 2012, we may resume offering similar products in the future.

- Identity Theft Protection. The most comprehensive identity theft monitoring product we offer includes an initial credit report, credit bureau report monitoring at the three major credit bureaus, prompt alerts to key changes to credit bureau files that help customers spot possible identity theft quickly, internet surveillance to monitor up to 20 credit and debit card numbers on suspicious websites, identity theft insurance up to $25,000 to cover certain out-of-pocket expenses due to identity theft, and access to knowledgeable professionals who can provide information about identity theft issues.
- Payment Protection. This product allows customers to suspend their payments for up to two years, depending on the qualifying event and product level, when certain qualifying life events occur. While on benefit, customers have no minimum monthly payment, and are not charged interest, late fees or the fees for the product. This product covers a variety of different events, such as unemployment, disability, natural disasters or other life events, such as marriage or birth of a child. Depending on the product and availability under state laws, outstanding balances up to $10,000 or $25,000, depending on product level are cancelled in the event of death.
- Wallet Protection. This product offers one-call convenience if a customer's wallet is lost or stolen, including requesting cancellation and replacement of the customer's credit and debit cards, monitoring the customer's credit bureau reports at the three major credit bureaus for 180 days and alerting them to key changes to their credit files, providing up to $100 to replace the customer's wallet or purse and, if needed, allowing the customer up to a $1,000 cash advance on his or her Discover card account.
- Credit ScoreTracker. This product offers customers resources that help them understand and monitor their credit scores. Credit ScoreTracker is specifically designed for score monitoring by alerting customers when their score changes, allowing customers to set a target score, and providing resources to help customers understand the factors that may be influencing their scores.

In addition to the protection products above, our credit card customers can purchase online service warranties from our extended warranty provider to protect purchases of new electronics and appliances as well as certain other purchases.

Brand and Advertising Management

We maintain a full-service marketing department charged with delivering integrated mass and direct communications to foster customer engagement with our products and services. Our brand team utilizes consumer insights and market

intelligence to define our mass communication strategy, create multi-channel advertising messages and develop marketing partnerships with sponsorship properties. This work is performed in house as well as with a variety of external agencies and vendors.

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Customer Service

Our customers can contact our customer service personnel by calling 1-800-Discover. Our customers can also manage their accounts online or through applications for certain mobile devices. Our internet and mobile solutions offer a range of benefits, including:

- Online account services that allow customers to customize their accounts, choose how and when they pay their bills, view annual account summaries that assist them with budgeting, research transaction details, initiate transaction disputes and chat with or email a customer representative;
- Email and mobile text reminders that help customers avoid fees, keep their accounts secure and track big purchases or returns;
- Money management tools like the Spend Analyzer, Paydown Planner and Purchase Planner; and
- An online portal where customers automatically earn 5-20% Cashback Bonus when they shop at well-known online merchants using their Discover card.

Our student loan, personal loan, home equity and deposit product customers can utilize our online account services to manage their accounts, and to use interactive tools and calculators. For the home loan origination process, we have an online portal for home loan customers to educate themselves on the home loan process, monitor the status of their loans prior to funding, upload documents and e-sign initial loan documents.

Processing Services

Our processing services cover four functional areas: card personalization/embossing, print/mail, remittance processing and document processing. Card personalization/embossing is responsible for the embossing and mailing of plastic credit cards for new accounts, replacements and reissues, and gift cards. Print/mail specializes in statement and letter printing and mailing for merchants and customers. Remittance processing, currently a function outsourced to third-party vendors, handles account payments and check processing. Document processing handles hard-copy forms, including new account applications.

Fraud Prevention

We monitor our customers' accounts to prevent, detect, investigate and resolve fraud. Our fraud prevention processes are designed to protect the security of cards, applications and accounts in a manner consistent with our customers' needs to easily acquire and use our products. Prevention systems monitor the authorization of application information, verification of customer identity, sales, processing of convenience and balance transfer checks, and electronic transactions.

Each credit card transaction is subject to screening, authorization and approval through a proprietary POS decision system. We use a variety of techniques that help identify and halt fraudulent transactions, including adaptive models, rules-based decision-making logic, report analysis, data integrity checks and manual account reviews. We manage accounts identified by the fraud detection system through technology that integrates fraud prevention and customer service. Strategies are subject to regular review and enhancement to enable us to respond quickly to changing conditions as well as to protect our customers and our business from emerging fraud activity.

Product Terms and Conditions

Credit Cards

The terms and conditions governing our credit card products vary by product and change over time. Each credit card customer enters into a cardmember agreement governing the terms and conditions of the customer's account. Discover card's terms and conditions are generally uniform from state to state. The cardmember agreement permits us, to the extent permitted by law, to change any term of the cardmember agreement, including any finance charge, rate or fee, or add or delete any term of the cardmember agreement, with notice to the customer as required by law. The customer has the right to opt out of certain changes of terms and pay their balance off under the original terms. Each cardmember agreement provides that the account can be used for purchases, cash advances and balance transfers. Each Discover card account is assigned a credit limit when the account is initially opened. Thereafter, individual credit limits may be increased or decreased from time to time, at our discretion, based primarily on our evaluation of the customer's creditworthiness. We offer various features and services with the Discover card accounts, including the Cashback Bonus rewards programs described under "— Marketing — Rewards/Cashback Bonus."

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All Discover card accounts generally have the same billing structure. We generally send a monthly billing statement to each customer who has an outstanding debit or credit balance. Customers also can waive their right to receive a physical copy of their bill, in which case they will receive email notifications of the availability of their billing statement online. Discover card accounts are grouped into multiple billing cycles for operational purposes. Each billing cycle has a separate billing date, on which we process and bill to customers all activity that occurred in the related accounts during a period of approximately 28 to 32 days that ends on the billing date.

Discover card accounts are assessed periodic finance charges using fixed and/or variable interest rates. Certain account balances, such as balance transfers, may accrue periodic finance charges at lower fixed rates for a specified period of time. Variable rates are indexed to the highest prime rate published in The Wall Street Journal on the last business day of the month. Periodic finance charges are calculated using the daily balance (including current transactions) method, which results in daily compounding of periodic finance charges, subject to a grace period on new purchases. The grace period essentially provides that periodic finance charges are not imposed on new purchases, or any portion of a new purchase, that is paid by the due date on the customer's current billing statement if the customer paid the balance on his or her previous billing statement in full by the due date on that statement. Neither cash advances nor balance transfers are subject to a grace period.

Each customer with an outstanding debit balance on his or her Discover card account must generally make a minimum payment each month. If a customer exceeds his or her credit limit as of the last day of the billing period, we may include all or a portion of this excess amount in the customer's minimum monthly payment. A customer may pay the total amount due at any time. We also may enter into arrangements with delinquent customers to extend or otherwise change payment schedules, and to waive finance charges and/or fees, including re-aging accounts in accordance with regulatory guidance.

In addition to periodic finance charges, we may impose other charges and fees on Discover card accounts, including cash advance transaction fees, late fees where a customer has not made a minimum payment by the required due date, balance transfer fees and returned payment fees. We also charge fees each time we decline to honor a balance transfer check, cash advance check, or other promotional check due to such reasons as insufficient credit availability, delinquency or default.

The Credit Card Accountability Responsibility and Disclosure Act of 2009 (the "CARD Act") required us to review, every six months, certain interest rates that were increased on accounts since January 1, 2009 to determine whether to reduce the interest rate based on the factors that prompted the increase or factors we currently consider in determining interest rates applicable to similar new credit card accounts. The amount of any rate decrease must be determined based upon our reasonable policies and procedures. Any reduced interest rate must be applied to the account not later than 45 days after completion of the review.

Student Loans

The terms and conditions governing our student loans vary by product and are specified in the borrower's promissory note and disclosures. Each borrower signs a promissory note and accepts the loan terms during the application process. Student loans feature zero origination fees, fixed or variable interest rates, and potential rewards. Student loans may include a deferment period, during which borrowers are not required to make payments while enrolled in school at least half time. This period begins on the date the loan is first disbursed and ends six to nine months after the borrower ceases to be enrolled in school at least half time. We also offer an optional "In-School Payment" product that requires a student to make monthly payments while in school. The standard repayment period is 15 to 20 years, depending on the type of student loan. Borrowers can choose to receive electronic communications, in which case they will receive email notifications of the availability of their monthly billing statements online. There is no prepayment penalty, and borrowers may decide whether or not to apply any excess payments toward their next monthly payments and advance their next due date.

We calculate interest on a daily basis on the outstanding principal loan balance until the loan is paid in full. The interest rate will never be higher than the maximum allowed by law, as stated in the promissory note and disclosures. The variable interest rate we offer, is equal to a variable index (e.g., based on the prime rate, London Interbank Offered Rate ("LIBOR") or T-Bill) plus a fixed margin assigned to the loan during origination. Variable interest rates may adjust quarterly if the index changes. We may impose other charges, including late charges when a customer has

not made a minimum payment by the required due date and a returned check charge. In certain circumstances, we may offer borrower assistance programs including forbearance periods of up to 12 months over the

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life of the loan or short-term payment reductions. We accrue interest when loans are in forbearance or in other payment assistance programs.

Personal Loans

The terms and conditions governing personal loans are set at the time the loan is accepted and generally do not change for the life of the loan. Personal loan account terms and conditions are generally uniform from state to state. All personal loan accounts generally have the same billing structure. Customers receive monthly statements approximately 20 days prior to payment due dates. The statement provides detail on all transactions processed since the last statement was generated, as well as a summary of the current amount due. Customers also can waive their right to receive physical copies of their bills, in which case they will receive email notifications of the availability of their billing statements online. Personal loan accounts are assessed periodic finance charges using simple interest. We may impose other charges, including late charges when a customer has not made a minimum payment by the required due date and a returned check charge. There is no prepayment penalty for repaying a personal loan balance in full prior to the scheduled maturity date.

Home Loans and Home Equity Loans

We offer prime adjustable, fixed-rate conforming, jumbo, FHA and VA first lien home loans to qualified applicants. The terms of the loan are set at closing. Substantially all funded loans and the related loan servicing rights are sold to investors in the secondary market, generally within 30 days of funding.

Home equity loans are fixed-rate loans that carry a monthly payment over the term of the loan and are secured by a first or second lien on a customer's home. The terms of the loan are set at closing. Customers are sent monthly statements 20 days in advance of the payment due date. The statements provide the customer the allocation of any payments made since the last billing date as well as the payment due on the next scheduled payment date. The customer has the ability to view their account information as well as make payments online through the account center. Customers are also subject to additional charges, including late fees and returned payment charges. The customer has the ability to make larger than minimum payments on the loans and early payoffs are not subject to a prepayment penalty.

Deposits

We offer four main types of deposit products directly to consumers on a national basis: certificates of deposit, savings accounts, money market and checking accounts, though at the current time we are offering checking accounts only to existing credit card or deposit customers. All of these deposits are FDIC insured to the maximum permitted by law. Interest is compounded daily and credited to each account on a monthly basis, using the daily balance method. We do not pay interest generally on checking account balances, but instead offer cashback rewards for certain transactions. We offer a range of ownership options, including single, joint, trust and custodial. Deposit accounts may be funded through electronic funds transfer, check or wire transfer. Customers may service their accounts through a variety of convenient methods, including online at www.discoverbank.com, mobile and tablet device applications, and by telephone.

Certificates of deposit are offered on a full range of tenors from three months through 10 years with interest rates that are fixed for the full period. We provide automatic renewal along with options on reinvestment or disbursement of interest. There are minimum balance requirements to open certificates of deposit and penalties for early withdrawals.

Money market accounts are transactional accounts with minimum balance requirements. Money market account funds may be accessed through electronic funds transfer, checks, wire transfer and debit cards. Savings accounts may be accessed through electronic funds transfer, wire transfer and official checks. Money market accounts and savings accounts have limitations on withdrawal frequency, as required by law. Interest rates on money market accounts and savings accounts are subject to change at any time. Fees apply to some transactions, and availability of funds varies based on product and method of funding.

We also issue certificates of deposit through select contracted brokerage firms. All of these deposits are also FDIC insured to the maximum allowed by law. All settlements occur through the Depository Trust Company. Tenors issued, interest and commission rates are determined weekly with tenor issuances of five months to ten years. Simple interest is applied to brokered certificates of deposit. At any given time, we may choose to not issue these certificates of deposit or to issue only certain tenors in a given week. Early redemption of these certificates occurs only in the event

of death or adjudication of incompetence. We have also entered into several third-party agreements which provide structured sweep deposit balances.

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Discover Network Operations

We support our merchants through a merchant acquiring model that includes direct relationships with large merchants in the United States and arrangements with merchant acquirers for small- and mid-size merchants. In addition to our U.S.-based merchant acceptance locations, Discover Network cards also are accepted at many locations in Canada, Mexico, the Caribbean, China, Japan and a growing number of countries around the world on the Diners Club network, or through reciprocal acceptance arrangements made with international payment networks (i.e., network-to-network).

We maintain direct relationships with most of our largest merchant accounts, which enables us to benefit from joint marketing programs and opportunities and to retain the entire discount revenue from the merchants. The terms of our direct merchant relationships are governed by merchant services agreements. These agreements also are accompanied by additional program documents that further define our network functionality and requirements, including operating regulations, technical specifications and dispute rules. To enable ongoing improvements in our network's functionality and in accordance with industry convention, we publish updates to our program documents on a semi-annual basis. Discover card transaction volume was concentrated among our top 100 merchants in the 2014 calendar year with our largest merchant accounting for approximately 8% of total Discover card transaction volume.

In order to increase merchant acceptance, Discover Network services the majority of its small- and mid-size merchant portfolios through third-party merchant acquirers to allow such acquirers to offer a comprehensive payments processing package to such merchants. Merchants also can apply to our merchant acquirer partners directly to accept Discover Network cards through the acquirers' integrated payments solutions. Merchant acquirers provide merchants with consolidated servicing for Discover, Visa and MasterCard transactions, resulting in streamlined statements and customer service for merchants, and reduced costs for us. These acquirer partners also perform credit evaluations and screen applications against unacceptable business types and the Office of Foreign Asset Control Specifically Designated Nationals list.

Discover Network operates systems and processes that seek to ensure data integrity, prevent fraud and ensure compliance with our operating regulations. Our systems evaluate incoming transaction activity to identify abnormalities that require investigation and fraud mitigation. Designated Discover Network personnel are responsible for validating compliance with our operating regulations and law, including enforcing our data security standards and prohibitions against illegal or otherwise unacceptable activities. Discover Network is a founding and current member of the Payment Card Industry Security Standards Council, LLC, and is working to expand the adoption of the Council's security standards globally for merchants and service providers that store, transmit or process cardholder data.

Technology

We provide technology systems processing through a combination of owned and hosted data centers and the use of third-party vendors. These data centers support our payment networks, provide customers with access to their accounts and manage transaction authorizations, among other functions. Discover Network works with a number of vendors to maintain our connectivity in support of POS authorizations. This connectivity also enables merchants to receive timely payment for their Discover Network card transactions.

Our approach to technology development and management involves both third-party and in-house resources. We use third-party vendors for basic technology services (e.g., telecommunications, hardware and operating systems) as well as for processing and other services for our direct banking and payment services businesses. We subject each vendor to a formal approval process to ensure that the vendor can assist us in maintaining a cost-effective and reliable technology platform. We use our in-house resources to build, maintain and oversee some of our technology systems. We believe this approach enhances our operations and improves cost efficiencies.

Seasonality

In our credit card business, we experience fluctuations in transaction volumes and the level of loan receivables as a result of higher seasonal consumer spending and payment patterns around the winter holidays, summer vacations and back-to-school periods. In our student loan business, our loan disbursements peak at the beginning of a school's academic semester or quarter. Although there is a seasonal impact to transaction volumes and the levels of credit card and student loan receivables, seasonal trends have not caused significant fluctuations in our results of operations or

credit quality metrics between quarterly and annual periods.

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Revenues in our Diners Club business are generally higher in the first half of the year as a result of Diners Club's tiered pricing system where licensees qualify for lower royalty rate tiers as cumulative volume grows during the course of the year.

Competition

We compete with other consumer financial services providers and payment networks on the basis of a number of factors, including brand, reputation, customer service, product offerings, incentives, pricing and other terms. Our credit card business also competes on the basis of reward programs and merchant acceptance. We compete for accounts and utilization with cards issued by other financial institutions (including American Express, Bank of America, JPMorgan Chase and Citi) and, to a lesser extent, businesses that issue their own private label cards or otherwise extend credit to their customers. In comparison to our largest credit card competitors, our strengths include cash rewards, conservative portfolio management and strong customer service. Competition based on cash rewards programs, however, has increased in recent years. Our student loan product competes for customers with Sallie Mae and Wells Fargo, as well as other lenders that offer student loans. Our personal loan product competes for customers primarily with JPMorgan Chase, Wells Fargo, Citi and peer to peer lenders. Our home loan product competes for customers primarily with traditional lending institutions, namely Wells Fargo, Bank of America, JPMorgan Chase and Citi, which operate in multiple distribution channels, including direct-to-consumer. Our home loan product also faces additional competition from direct lending websites owned and operated by other online lenders that originate the bulk of their loans through their websites or by phone. Our home equity product faces competition primarily from traditional branch lending institutions like Wells Fargo, JP Morgan Chase, U.S. Bank and PNC.

Although our student and personal loan receivables have increased, our credit card receivables continue to represent most of our receivables. The credit card business is highly competitive. Some of our competitors offer a wider variety of financial products than we do, including automobile loans, which may currently position them better among customers who prefer to use a single financial institution to meet all of their financial needs. Some of our competitors enjoy greater financial resources, diversification and scale than we do, and are therefore able to invest more in initiatives to attract and retain customers, such as advertising, targeted marketing, account acquisitions and pricing offerings in interest rates, annual fees, reward programs and low-priced balance transfer programs. In addition, some of our competitors have assets such as branch locations and co-brand relationships that may help them compete more effectively. Another competitive factor in the credit card business is the increasing use of debit cards as an alternative to credit cards for purchases.

Because most domestically-issued credit cards, other than those issued on the American Express network, are issued on the Visa and MasterCard networks, most other card issuers benefit from the dominant market share of Visa and MasterCard. The former exclusionary rules of Visa and MasterCard limited our ability to attract merchants and credit and debit card issuers, contributing to Discover not being as widely accepted in the U.S. as Visa and MasterCard. Merchant acceptance of the Discover card has increased in the past several years, both in the number of merchants enabled for acceptance and the number of merchants actively accepting Discover. We continue to make investments in expanding Discover and Diners Club acceptance in key international markets where an acceptance gap exists.

In our payment services business, we compete with other networks for volume and to attract network partners to issue credit, debit and prepaid cards on the Discover, PULSE and Diners Club networks. We generally compete on the basis of customization of services and various pricing strategies, including incentives and rebates. We also compete on the basis of issuer fees, fees paid to networks (including switch fees), merchant acceptance, network functionality, customer perception of service quality, brand image, reputation and market share. The Diners Club and Discover networks' primary competitors are Visa, MasterCard and American Express, and PULSE's network competitors include Visa's Interlink, MasterCard's Maestro and First Data's STAR. American Express is a particularly strong competitor to Diners Club as both cards target international business travelers. As the payments industry continues to evolve, we are also facing increasing competition from new entrants to the market, such as online networks, telecom providers and other alternative payment providers, which leverage new technologies and a customer's existing deposit and credit card accounts and bank relationships to create payment or other fee-based solutions.

In our direct-to-consumer deposits business, we have acquisition and servicing capabilities similar to other direct competitors, including USAA, Ally Bank, American Express, Capital One (360), Sallie Mae and Barclays. We also

compete with traditional banks and credit unions that source deposits through branch locations. We seek to differentiate our deposit product offerings on the basis of brand reputation, convenience, customer service and value.

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For more information regarding the nature of and the risks we face in connection with the competitive environment for our products and services, see "Risk Factors — Strategic Business Risk."

Intellectual Property

We use a variety of methods, such as trademarks, patents, copyrights and trade secrets, to protect our intellectual property. We also place appropriate restrictions on our proprietary information to control access and prevent unauthorized disclosures. Our Discover, PULSE and Diners Club brands are important assets, and we take steps to protect the value of these assets and our reputation.

Employees

As of January 31, 2015, we employed approximately 14,676 individuals.

Risk Management

Our business exposes us to strategic (including reputational), credit, market, liquidity, operational, compliance and legal risks. We use a comprehensive enterprise-wide risk management framework to identify, measure, monitor, manage and report on risks we assume in conducting our activities. We seek financial returns commensurate with the risks to which we are exposed.

Enterprise Risk Management Principles

Our enterprise risk management philosophy is expressed through five key principles that guide our approach to risk management: comprehensiveness, accountability, independence, defined risk appetite and transparency.

Comprehensiveness

We seek to maintain a comprehensive framework for managing risk enterprise-wide, including policies, risk management processes, monitoring and testing, and reporting. Our framework is designed to be comprehensive with respect to our reporting segments and their control and support functions, and it extends across all risk types.

Accountability

We structure accountability across three lines of defense along the principles of risk management execution, oversight and independent validation. As the first line of defense, our business units seek to proactively manage the risks to which they are exposed as a result of their activities. Employees are expected to identify, report and correct process weaknesses.

Independence

Our second and third lines of defense, which are comprised of risk and control functions, operate independent of the business units. The second line of defense includes our corporate risk management ("CRM") department, which is led by our Chief Risk Officer (“CRO”), who is appointed by our Board of Directors. The CRO is accountable for providing an independent perspective on the risks to which we are exposed and how well management is identifying, assessing and managing risk; and the capabilities we have to manage risk across the enterprise. Our internal audit department, as the third line of defense, performs periodic, independent reviews and tests compliance with risk management policies, procedures and standards across the Company.

Defined Risk Appetite

We operate within the risk appetite framework approved by our Board of Directors, which guides an acceptable level of risk taking, considering desired financial returns and other objectives. To that end, limits and escalation thresholds are set consistent with the risk appetite approved by our Board of Directors.

Transparency

We seek to provide transparency of exposures and outcomes, which is core to our risk culture and operating style. We provide this risk transparency through our risk committee structure and standardized processes for escalating issues and reporting. This is accomplished at several levels within the organization, including monthly meetings held by our Risk Committee and quarterly reports to the Risk Oversight Committee of our Board of Directors, as well as regular

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reporting to our Risk subcommittees commensurate with the needs of our businesses. Further, the CRO is a member of the Executive Committee.

Risk Management Roles and Responsibilities

Our governance structure is designed and will be adjusted as necessary to meet the continuous needs of the business, and based on the principle that each line of business is responsible for managing risks inherent in its business with appropriate independent oversight and assessment. Committees are in place to oversee the management of risks across the Company. We seek to apply operating principles consistently to each committee. These operating principles are detailed in committee charters, which are approved by our Risk Committee.

Board of Directors

Our Board of Directors is responsible for: (i) approval of certain risk management policies, (ii) approval of our capital targets and risk appetite and associated limits, (iii) oversight of our strategic plan and (iv) appointment of our CRO.

Risk Oversight Committee of our Board of Directors

Our Risk Oversight Committee of our Board of Directors is responsible for reviewing and approving the risk management policies and overseeing the operations of our enterprise-wide risk management framework. Our Risk Oversight Committee approves risk management policies, oversees the operation of policies and procedures, and reviews reports from management on the status of and changes to risk exposures. In addition, our Risk Oversight Committee is responsible for the oversight of capital planning, liquidity risk management and resolution planning activities.

Risk Committee

Our Risk Committee is an executive management-level committee, that establishes a comprehensive risk management program and provides a forum to review and discuss credit, market, liquidity, operational, compliance and legal, and strategic risks across the Company and for each business unit. Risk Committee membership includes all members of our Executive Committee. The Committee establishes policies and reviews effectiveness of procedures to identify, measure, monitor, manage and report risk enterprise-wide, communicates risk appetite and philosophy, and reviews aggregated risk exposures within the Company. The Committee provides periodic reports to our Risk Oversight and Audit Committees.

Our Risk Committee has formed and designated a number of committees to assist it in carrying out its responsibilities. These committees, made up of representatives from senior levels of management, escalate issues to our Risk Committee as guided by escalation thresholds. These risk management committees include the Discover Bank Credit Committee, Asset/Liability Management Committees (Discover Financial Services and Discover Bank), the Counterparty Credit Committee, the New Initiatives Committee, the Operational Risk Committee, the Capital Planning Committee, and the Compliance Committee.

Chief Executive Officer (“CEO”)

The CEO is ultimately responsible for risk management within our Company. In that capacity, the CEO oversees the CRO, establishes a risk management culture throughout the Company and ensures that businesses operate in accordance with this risk culture.

Business Unit Heads

Our executive committee members, as business unit heads, are responsible for managing risk in pursuit of their strategic, financial and other business objectives, and ensuring their business units operate within established risk appetite limits. They are also responsible for identifying risks and implementing appropriate controls; explicitly considering risk when developing strategic plans, budgets and new products; and implementing appropriate risk controls when pursuing business strategies and objectives. Senior executive officers also coordinate with our CRM department to produce relevant, sufficient, accurate and timely risk reporting that is consistent with the processes and methodology established by our CRM department. In addition, our business unit heads are responsible for ensuring that sufficient financial resources and qualified personnel are deployed to manage the risks inherent in our business

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activities. Additionally, our business unit heads designate, in consultation with the CRO, a business risk officer to assist with risk management responsibilities.
Business risk officers work in conjunction with the business unit head to implement a business risk management program that satisfies business unit needs and adheres to corporate policy, standards and risk architecture.

Chief Risk Officer

Our CRO is a member of the Executive Committee and chairs our Risk Committee. In addition, the CRO has oversight responsibility to establish the CRM function with capabilities to exercise its mandate across all risk categories. Our CRO reports directly to our Risk Oversight Committee and administratively to the CEO. The CRO provides an independent view on the key risks to which our Company is exposed to our Risk Committee, our Audit Committee, our Risk Oversight Committee and our Board of Directors.

Corporate Risk Management

CRM is led by the CRO and supports business units by providing objective oversight of our risk profile to help ensure that risks are managed, aggregated and reported to our Risk Committee, our Risk Oversight Committee and our Audit Committee. CRM participates in our Risk Committee and sub-committee meetings to provide an enterprise-wide perspective on risk, governance matters, policies and risk thresholds. CRM is comprised of operational, consumer credit, counterparty credit, and market and liquidity risk oversight functions. In addition, CRM has enterprise risk management, corporate compliance, third-party risk management, and risk and insurance management frameworks to manage potential risk that might arise within these respective areas.

Law Department

Our law department plays a significant role in managing our legal risk, policy development and training, and in collaborating with the business units to incorporate a commitment to compliance in our day-to-day activities. The law department participates in meetings of our Risk Committee and the risk subcommittees in order to advise on legal and regulatory matters.

Internal Audit Department

Our internal audit department performs periodic, independent reviews and testing of compliance with risk management policies and standards across the Company, as well as assessments of the design and operating effectiveness of these policies and standards. The internal audit department also validates that risk management controls are functioning as intended by reviewing and evaluating the design and operating effectiveness of the CRM program and processes, including the independence and effectiveness of the CRM function. The results of such reviews are reported to our Audit Committee.

Risk Appetite and Strategic Limit Structure

Risk appetite is defined as the aggregate level in the type of risks we are willing to accept or avoid in order to achieve our strategic objectives, reflecting and based on our risk management philosophy and current business model that, in turn, influences our culture and operating style. The determination of risk appetite is directly linked to the strategic and capital planning process and is consistent with our aspirations and mission statement. The expressions of risk appetite also serve as tools to preclude business activities that are inconsistent with our long-term goals.
We segment our risk appetite expressions by type and cascading approval levels. Our Board of Directors approves our risk appetite and strategic limit structure, our Risk Committee approves our tactical limits and escalation triggers, and our risk sub-committees establish our execution-level limits.
Management and our CRM department monitor approved limits and escalation triggers to ensure that the business is operating within the expressed risk appetite and limits. Risk limits are monitored and reported on to various risk committees and our Board of Directors, as appropriate. Through ongoing monitoring of risk exposures, management is able to identify appropriate risk response and mitigation strategies in order to react dynamically to changing conditions.

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Risk Categories

We are exposed to a broad set of risks in the course of our business activities due to both internal and external factors, which we segment into six major risk categories. The first five are defined to be broadly consistent with Federal Reserve regulatory guidance and Basel: credit, market, liquidity, operational, and compliance/legal risk. We recognize the sixth, strategic risk, as a separate risk category. We evaluate the potential impact of a risk event on the Company by assessing the financial impact, the impact to our reputation, the legal and regulatory impact, and the client/customer impact. In addition, we have established various policies to help govern these risks.

Credit Risk

Credit risk arises from the potential that a borrower or counterparty will fail to perform on an obligation. Our credit risk includes consumer credit risk and counterparty credit risk. Consumer credit risk is primarily incurred by Discover Bank through the issuance of (i) unsecured credit including credit cards, student loans and personal loans and (ii) secured credit including secured credit cards, deposit secured loans and home equity loans. Discover Home Loans incurs consumer credit risk through the issuance of residential first mortgage loans to consumers. Commercial credit risk and residential first mortgage loans originated by Discover Bank are limited to certain Community Reinvestment Act ("CRA") compliance activities and the issuance of small business credit cards. Counterparty credit risk is incurred through a number of activities including settlement, certain marketing programs, treasury and asset/liability management, network incentive programs, vendor relationships and insurers.

The Discover Bank Credit Committee ensures the lending activities of the Bank comply with the Bank Credit Policy and also identifies, measures, monitors and controls risk arising from consumer credit risk and commercial credit risk associated with small business credit cards. Risks associated with CRA activities are overseen and monitored by the CRA Committee of the Bank.

Our Counterparty Credit Committee is responsible for the enterprise-wide approach to counterparty credit risk management through development of the Counterparty Credit Risk Management Policy and the associated oversight framework for the identification, measurement, monitoring, managing and reporting of counterparty credit risk.

Market Risk

Market risk is the risk to our financial condition resulting from adverse movements in market rates or prices, such as interest rates, foreign exchange rates, credit spreads or equity prices. We are exposed to various types of market risk, in particular interest rate risk and other risks that arise through the management of our investment portfolio. The Asset/Liability Management Policy governs the management of market risk.

Liquidity Risk

Liquidity risk is the risk that we will be unable to meet our obligations as they become due because of an inability to liquidate assets or obtain adequate funding, or an inability to easily unwind or offset specific exposures without significantly lowering market prices because of inadequate market depth or market disruptions. The Asset/Liability Management Policy governs the management of liquidity risk.

Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk is inherent in all our businesses. Operational risk categories incorporate all of the operational loss event-type categories set forth by the Basel Committee on Banking Supervision, which include the following: (i) fraud (internal and external), (ii) employment practices and workplace safety, (iii) clients, products and business practices, (iv) damage to physical assets, (v) business disruption and system failures, and (vi) execution, delivery and process management.

Compliance and Legal Risk

Compliance risk is the operational risk of legal or regulatory sanctions, financial loss or damage to reputation resulting from failure to comply with laws, regulations, rules, other regulatory requirements, or codes of conduct and other standards of self-regulatory organizations applicable to us. Legal risk arises from the potential that unenforceable contracts, lawsuits or adverse judgments can disrupt or otherwise negatively affect our operations or condition. These risks are inherent in all of our businesses. Both compliance and legal risk are subsets of operational risk but are

recognized together as a separate and complementary risk category by us given their importance and the specific capabilities and resources we deploy to manage these risk types effectively.

Compliance and legal risk exposures are actively and primarily managed by our business units in conjunction with our compliance and law departments. Our compliance program governs the management of compliance risk. Our Risk Committee and Compliance Committee oversee our compliance and legal risk management. Our compliance and law departments provide independent oversight for all of our compliance and legal risk management activities. Our law department coordinates with our CRM and compliance departments in the management of compliance and legal risks by reporting and escalating material incidents, participating in risk and control self-assessments, and monitoring and reporting key risk indicators.

Strategic Risk

Strategic risk can arise from: adverse business decisions; improper implementation of decisions; and a failure to anticipate and respond to industry changes, create and maintain a competitive business model, and attract and profitably serve clients.

Our Executive Committee actively manages strategic risk through the development, implementation and oversight of our business strategies, including the development of budgets and business plans. Our business units take on and are accountable for managing strategic risk in pursuit of their objectives.

The New Initiative Policy and the Capital and Dividends Policy govern the management of strategic risk. In addition, the assessment of strategic risk is an important consideration of various subcommittees of our Risk Committee including the Discover Bank Credit Committee, our Asset and Liability Management Committee, our Capital Planning Committee and our New Initiative Committee. Our CRM department also plays an important role in the management of strategic risk by: (i) overseeing the objective setting and strategic planning processes from a risk perspective, to gain comfort that strategic risks have been adequately considered in the setting of objectives and development of strategies; (ii) providing an independent risk perspective to the new initiatives process; and (iii) assessing if there is effective alignment of management's proposed long-term strategic objectives with the risk appetite limits approved by our Board of Directors.

Capital Planning

Our capital planning and management framework encompasses forecasting capital levels, establishing capital targets, monitoring capital adequacy against targets, maintaining appropriate contingency capital plans and identifying strategic options to deploy excess capital.

Risk Management Review of Compensation

We believe in a pay for performance philosophy which considers performance across the company, business segments and individual performance, as appropriate, and the long-term interests of our shareholders and the safety and soundness of the Company. We design compensation to be competitive relative to our peers to attract, retain and motivate our employees. In addition to being competitive in the markets in which we compete for talent and encouraging employees to achieve objectives set out by our management, our compensation programs are designed to balance an appropriate mix of compensation components to align the interests of employees with the long-term interests of shareholders and the safety and soundness of the Company.

The design and administration of our compensation programs provide incentives that appropriately balance risk and financial results in a manner that does not incentivize employees to take imprudent risks, is compatible with effective controls and enterprise-wide risk management, and is supported by strong corporate governance, including oversight by our Board of Directors and the Compensation and Leadership Development Committee of our Board of Directors.

Supervision and Regulation

General

Our operations are subject to extensive regulation, supervision and examination under U.S. federal, state and foreign laws and regulations. As a bank holding company under the Bank Holding Company Act of 1956 and a financial holding company under the Gramm-Leach-Bliley Act, we are subject to the supervision, examination and

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regulation of the Federal Reserve. As a large provider of consumer financial services, we are subject to the supervision, examination and regulation of the Consumer Financial Protection Bureau (the "CFPB").

We operate two banking subsidiaries, each of which is in the United States. Discover Bank, our main banking subsidiary, offers credit card loans, student loans, personal loans and home equity loans as well as certificates of deposit, savings and checking accounts and other types of deposit accounts. Discover Bank is chartered and regulated by the Office of the Delaware State Bank Commissioner (the "Delaware Commissioner"), and is also regulated by the Federal Deposit Insurance Corporation (the "FDIC"), which insures its deposits up to applicable limits and serves as the bank's primary federal banking regulator. Our other bank, Bank of New Castle, is also chartered and regulated by the Delaware Commissioner and insured and regulated by the FDIC.

Bank Holding Company Regulation

Permissible activities for a bank holding company include those activities that are so closely related to banking as to be a proper incident thereto, such as consumer lending and other activities that have been approved by the Federal Reserve by regulation or order. Certain servicing activities are also permissible for a bank holding company if conducted for or on behalf of the bank holding company or any of its affiliates. Impermissible activities for bank holding companies include activities that are related to commerce such as retail sales of nonfinancial products.

A financial holding company and the non-bank companies under its control are permitted to engage in activities considered financial in nature, incidental to financial activities, or complementary to financial activities, if the Federal Reserve determines that such activities pose no risk to the safety or soundness of depository institutions or the financial system in general. Being a financial holding company under the Gramm-Leach-Bliley Act requires that the depository institutions that we control meet certain criteria, including capital, management and Community Reinvestment Act requirements. In addition, under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") we are required to meet certain capital and management criteria to maintain our status as a financial holding company. Failure to meet the criteria for financial holding company status results in restrictions on new financial activities or acquisitions and could require discontinuance of existing activities that are not generally permissible for bank holding companies.

Federal Reserve regulations and the Federal Deposit Insurance Act (the "FDIA"), as amended by the Dodd-Frank Act, require that bank holding companies serve as a source of strength to each subsidiary bank and commit resources to support each subsidiary bank. This support may be required at times when a bank holding company may not be able to provide such support without adversely affecting its ability to meet other obligations.

The Dodd-Frank Act addresses risks to the economy and the payments system, especially those posed by large systemically significant financial firms. Bank holding companies with $50 billion or more in total consolidated assets, including Discover, are considered systemically significant under the Dodd-Frank Act and are subject to heightened prudential standards established by the Federal Reserve. Regulatory developments, findings and ratings could negatively impact our business strategies or require us to: limit or change our business practices, restructure our products in ways that we may not currently anticipate, limit our product offerings, invest more management time and resources in compliance efforts, limit the fees we can charge for services, or limit our ability to pursue certain business opportunities and obtain related required regulatory approvals. For additional information regarding bank regulatory limitations on acquisitions and investments, see "— Acquisitions and Investments." See Note 19: Litigation and Regulatory Matters to our consolidated financial statements for more information on recent matters affecting Discover. Regulatory developments could also impact our strategies, the value of our assets, or otherwise adversely affect our businesses. For more information regarding the regulatory environment and developments under the Dodd-Frank Act, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments" and “Risk Factors."

Capital, Dividends and Share Repurchases

We, Discover Bank and Bank of New Castle are subject to capital adequacy guidelines adopted by federal banking regulators, which include maintaining minimum capital and leverage ratios for capital adequacy and higher ratios to be deemed "well-capitalized." As a bank holding company, we were required to maintain Tier 1 and total capital equal to at least 4% and 8% of our total risk-weighted assets, respectively, prior to January 1, 2015. We were also required to maintain a minimum "leverage ratio" (Tier 1 capital to adjusted total assets) of 4% to 5% prior to January 1, 2015,

depending upon criteria defined and assessed by the Federal Reserve. Further, under the Federal Reserve's annual capital plan requirements, we are required to demonstrate that under stress scenarios we will maintain

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a Tier 1 common ratio (meaning the ratio of Tier 1 common capital to total risk-weighted assets) above 5%. At December 31, 2014, Discover Financial Services met all requirements to be deemed "well-capitalized." For related information regarding our bank subsidiaries, see "— FDIA" below.

Federal Reserve and FDIC final rules applicable to Discover Financial Services and Discover Bank, respectively, include new minimum and "well-capitalized" risk-based capital and leverage ratios, effective January 1, 2015, and refine the definition of what constitutes "capital" for purposes of calculating those ratios. The new minimum capital level requirements applicable to Discover Financial Services and Discover Bank under the final rules, beginning January 1, 2015, are: (i) a new common equity Tier 1 capital ratio of 4.5%; (ii) a Tier 1 risk-based capital ratio of 6% (increased from 4%); (iii) a total risk-based capital ratio of 8% (unchanged); and (iv) a Tier 1 leverage ratio of 4% for all U.S. banking institutions. The new capital level requirements to be “well-capitalized” under the final rules are: (i) a common equity Tier 1 capital ratio of 6.5%; (ii) a Tier 1 risk-based capital ratio of 8%; (iii) a total risk-based capital ratio of 10%; and (iv) a Tier 1 leverage ratio of 5%.

There are various federal and state law limitations on the extent to which our banking subsidiaries can provide funds to us through dividends, loans or otherwise. These limitations include minimum regulatory capital requirements, federal and state banking law requirements concerning the payment of dividends out of net profits or surplus, and general federal and state regulatory oversight to prevent unsafe or unsound practices. In general, federal and applicable state banking laws prohibit, without first obtaining regulatory approval, insured depository institutions, such as our banking subsidiaries, from making dividend distributions if such distributions are not paid out of available earnings or would cause the institution to fail to meet applicable capital adequacy standards. For more information, see "— FDIA" below.

Additionally, we are required to submit an annual capital plan to the Federal Reserve that includes an assessment of our expected uses and sources of capital over the nine quarter planning horizon. In January 2015, we submitted our annual capital plan to the Federal Reserve under the Federal Reserve’s Comprehensive Capital Analysis and Review, or CCAR, program, which included planned dividends and share repurchases over the nine quarter planning horizon. Our ability to make capital distributions, including our ability to pay dividends or repurchase shares of our common stock, will be subject to the Federal Reserve's review and non-objection of the actions that we proposed in our annual capital plan. In addition, Discover Financial Services is required to publish company-run stress tests results in March and September each year in accordance with Federal Reserve rules and Discover Bank is required to publish company-run stress test results under FDIC rules. The dates for publication of stress test results by Discover Financial Services and Discover Bank may differ after 2015 based on recently updated rules adopted by the Federal Reserve and the FDIC.

For more information, including additional conditions and limits on our ability to pay dividends and repurchase our stock, see "Risk Factors — Credit, Market and Liquidity Risk — We may be limited in our ability to pay dividends on and repurchase our stock" and "— We are a holding company and depend on payments from our subsidiaries," "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Capital" and Note 17: Capital Adequacy to our consolidated financial statements.

FDIA

The FDIA imposes various requirements on insured depository institutions. For example, the FDIA requires, among other things, the federal banking agencies to take "prompt corrective action" in respect of depository institutions that do not meet minimum capital requirements. The FDIA sets forth the following five capital tiers: "well-capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized." A depository institution's capital tier will depend upon how its capital levels compare with various relevant capital measures and certain other factors that are established by regulation. At December 31, 2014, Discover Bank and Bank of New Castle met all applicable requirements to be deemed "well-capitalized." As noted above, recently-issued Federal Reserve rules and additional future rulemaking, including with respect to implementation of Basel III, have altered and in the future could further alter the capital adequacy framework for Discover.

The FDIA also prohibits any depository institution from making any capital distributions (including payment of a dividend) or paying any management fee to its parent holding company if the depository institution would thereafter be "undercapitalized." "Undercapitalized" institutions are subject to growth limitations and are required to submit a

capital restoration plan. For a capital restoration plan to be acceptable, among other things, the depository institution's parent holding company must guarantee that the institution will comply with the capital restoration plan.

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If a depository institution fails to submit an acceptable capital restoration plan, it is treated as if it is "significantly undercapitalized." "Significantly undercapitalized" depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become "adequately capitalized," requirements to reduce total assets, and cessation of receipt of deposits from correspondent banks. "Critically undercapitalized" institutions are subject to the appointment of a receiver or conservator.

Each of our banking subsidiaries may also be held liable by the FDIC for any loss incurred, or reasonably expected to be incurred, due to the default of the other U.S. banking subsidiary and for any assistance provided by the FDIC to the other U.S. banking subsidiary that is in danger of default.

The FDIA prohibits insured banks from accepting brokered deposits or offering interest rates on any deposits significantly higher than the prevailing rate in the bank's normal market area or nationally (depending upon where the deposits are solicited), unless it is "well-capitalized," or it is "adequately capitalized" and receives a waiver from the FDIC. A bank that is "adequately capitalized" and that accepts brokered deposits under a waiver from the FDIC may not pay an interest rate on any such deposit in excess of 75 basis points over certain prevailing market rates. There are no such restrictions under the FDIA on a bank that is "well-capitalized." As of December 31, 2014, Discover Bank and Bank of New Castle each met the FDIC's definition of a "well-capitalized" institution for purposes of accepting brokered deposits. An inability to accept brokered deposits in the future could materially adversely impact our funding costs and liquidity. For more information, see “Risk Factors — Credit, Market and Liquidity Risk — An inability to accept or maintain deposits in the future could materially adversely affect our liquidity position and our ability to fund our business.”

The FDIA also affords FDIC-insured depository institutions, such as Discover Bank and Bank of New Castle, the ability to "export" favorable interest rates permitted under the laws of the state where the bank is located. Discover Bank and Bank of New Castle are both located in Delaware and, therefore, charge interest on loans to out-of-state borrowers at rates permitted under Delaware law, regardless of the usury limitations imposed by the state laws of the borrower's residence. Delaware law does not limit the amount of interest that may be charged on loans of the type offered by Discover Bank or Bank of New Castle. This flexibility facilitates the current nationwide lending activities of Discover Bank and Bank of New Castle.

The FDIA subjects Discover Bank to deposit insurance assessments. Under the Dodd-Frank Act, in order to bolster the reserves of the Deposit Insurance Fund, the minimum reserve ratio set by the FDIC was increased to 1.35%. The FDIC set a reserve ratio of 2%, 65 basis points above the statutory minimum. The FDIC also amended its deposit insurance regulations with two changes. First, the FDIC implemented a provision of the Dodd-Frank Act that changed the assessment base for deposit insurance premiums from one based on domestic deposits to one based on average consolidated total assets minus average tangible equity. Second, the FDIC revised the risk-based assessment system for all large insured depository institutions (generally, institutions with at least $10 billion in total assets, including Discover Bank) to one based on a scorecard method. Further increases may occur in the future. The Dodd-Frank Act removed the statutory cap for the reserve ratio, leaving the FDIC free to set a cap in the future.

Acquisitions and Investments

Since we are a bank holding company, and Discover Bank and Bank of New Castle are insured depository institutions, we are subject to banking laws and regulations that limit the types of acquisitions and investments that we can make. In addition, certain permitted acquisitions and investments that we seek to make are subject to the prior review and approval of our banking regulators, including the Federal Reserve and FDIC. Our banking regulators have broad discretion on whether to approve proposed acquisitions and investments. In deciding whether to approve a proposed acquisition, federal bank regulators will consider, among other factors, the effect of the acquisition on competition, our financial condition, and our future prospects, including current and projected capital ratios and levels; the competence, experience, and integrity of our management and our record of compliance with laws and regulations; the convenience and needs of the communities to be served, including our record of compliance under the Community Reinvestment Act; and our effectiveness in combating money laundering. Therefore, results of supervisory activities of the banking regulators, including examination results and ratings, can impact whether regulators approve proposed acquisitions and investments. Supervisory actions related to anti-money laundering and related laws and regulations will limit for a period of time our ability to enter into certain types of acquisitions and make certain types of

investments. For more information on recent matters affecting Discover, see Note 19: Litigation and Regulatory Matters to our consolidated financial statements. For information on the challenging regulatory environment, see "Risk Factors."

In addition, certain acquisitions of our voting stock may be subject to regulatory approval or notice under U.S. federal or Delaware state law. Investors are responsible for ensuring that they do not, directly or indirectly, acquire shares of our stock in excess of the amount that can be acquired without regulatory approval under the Change in Bank Control Act, the Bank Holding Company Act and the Delaware Change in Bank Control provisions, which prohibit any person or company from acquiring control of us without, in most cases, the prior written approval of each of the FDIC, the Federal Reserve and the Delaware Commissioner.

Consumer Financial Services

The relationship between us and our U.S. customers is regulated extensively under federal and state consumer protection laws. Federal laws include the Truth in Lending Act, the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Gramm-Leach-Bliley Act, the CARD Act and the Dodd-Frank Act. These and other federal laws, among other things, prohibit unfair, deceptive and abusive trade practices, require disclosures of the cost of credit, provide substantive consumer rights, prohibit discrimination in credit transactions, regulate the use of credit report information, provide financial privacy protections, require safe and sound banking operations, restrict our ability to raise interest rates, and subject us to substantial regulatory oversight. The CFPB has rulemaking and interpretive authority under the Dodd-Frank Act and other federal consumer financial services laws, as well as broad supervisory, examination and enforcement authority over large providers of consumer financial products and services, such as Discover. For more information, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments — Consumer Financial Services."

State and, in some cases, local laws also may regulate in these areas, as well as in the areas of collection practices, and may provide other additional consumer protections. Moreover, our U.S. subsidiaries are subject to the Servicemembers Civil Relief Act, which protects persons called to active military service and their dependents from undue hardship resulting from their military service. The Servicemembers Civil Relief Act applies to all debts incurred prior to the commencement of active duty (including credit card and other open-end debt) and limits the amount of interest, including service and renewal charges and any other fees or charges (other than bona fide insurance) that is related to the obligation or liability.

Violations of applicable consumer protection laws can result in significant potential liability in litigation by customers, including civil monetary penalties, actual damages, restitution and attorneys' fees. Federal banking regulators, as well as state attorneys general and other state and local consumer protection agencies, also may seek to enforce consumer protection requirements and obtain these and other remedies. Further violations may cause federal banking regulators to deny, or delay approval of, potential acquisitions and investments. See "— Acquisitions and Investments."

We are subject to additional laws and regulations affecting mortgage lenders. We conduct our mortgage lending business through two subsidiaries: Discover Bank (for our home equity loans) and Discover Home Loans, Inc. (for our conventional refinances and purchase transactions), which is a state-licensed mortgage lender. Federal, state and, in some instances, local laws regulate mortgage lending activities. These laws generally regulate the manner in which lending and lending-related activities are marketed or made available, including advertising and other consumer disclosures, payments for services and recordkeeping requirements. These laws include the Real Estate Settlement Procedures Act, the Fair Credit Reporting Act, the Truth in Lending Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Home Mortgage Disclosure Act and various state laws. State laws often restrict the amount of interest and fees that may be charged by a mortgage lender, or otherwise regulate the manner in which mortgage lenders operate or advertise. The CFPB has indicated that the mortgage industry is an area of supervisory focus and that it will concentrate its examination and rulemaking efforts on the variety of mortgage-related topics required under the Dodd-Frank Act, including the steering of consumers to less favorable products, discrimination, abusive or unfair lending practices, predatory lending, origination disclosures, minimum mortgage underwriting standards, mortgage loan origination compensation and servicing practices. The CFPB has published several final rules impacting the mortgage industry. For more information, see “Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments — Consumer Financial Services — Mortgage Lending.”

Payment Networks

We operate the Discover and PULSE networks, which deliver switching and settlement services to financial institutions and other program participants for a variety of ATM, POS and other electronic banking transactions. These operations are regulated by certain federal and state banking, privacy and data security laws. Moreover, the Discover and PULSE networks are subject to examination under the oversight of the Federal Financial Institutions Examination

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Council, an interagency body composed of the federal bank regulators and the National Credit Union Association. In addition, as our payments business has expanded globally through Diners Club, we are subject to government regulation in countries in which our networks operate or our cards are used, either directly or indirectly through regulation affecting Diners Club network licensees. Changes in existing federal, state or international regulation could increase the cost or risk of providing network services, change the competitive environment, or otherwise materially adversely affect our operations. The legal environment regarding privacy and data security is particularly dynamic, and any unpermitted disclosure of confidential customer information could have a material adverse impact on our business, including loss of consumer confidence.

The Dodd-Frank Act contains several provisions that are relevant to the business practices, network transaction volume, revenue and prospects for future growth of PULSE, our debit card network business. The Dodd-Frank Act requires that merchants control the routing of debit transactions, and that interchange fees received by certain payment card issuers on debit card transactions be “reasonable and proportional” to the issuer's cost in connection with such transactions, as determined by the Federal Reserve. The Dodd-Frank Act also requires the Federal Reserve to restrict debit card networks and issuers from requiring debit card transactions to be processed solely on a single payment network or two or more affiliated networks, or from requiring that transactions be routed over certain networks. For information regarding related impacts on our debit card business, see “Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments — Payment Networks.”

Money Laundering & Terrorist Financing Prevention Program

We maintain an enterprise-wide program designed to comply with all applicable anti-money laundering and anti-terrorism laws and regulations, including the Bank Secrecy Act and the USA PATRIOT Act of 2001. This program includes policies, procedures, training and other internal controls designed to mitigate the risk of money laundering or terrorist financing posed by our products, services, customers and geographic locale. These controls include procedures and processes to detect and report suspicious transactions, perform customer due diligence, and meet all recordkeeping and reporting requirements related to particular transactions involving currency or monetary instruments. The program is coordinated by a compliance officer and undergoes an annual independent audit to assess its effectiveness. Our program is typically reviewed on an annual basis by federal banking regulators. In June 2014, Discover Bank entered into a Consent Order with the FDIC to resolve matters related to the FDIC’s examination of Discover Bank’s anti-money laundering and related compliance programs. In the Consent Order, Discover Bank agreed to, among other things, enhance its anti-money laundering and related compliance programs. Also, the Federal Reserve notified us of its intention to enter into a supervisory action with us to require enhancements to our enterprise-wide anti-money laundering and related compliance programs. See Note 19: Litigation and Regulatory Matters to our consolidated financial statements for more information. For additional information regarding bank regulatory limitations on acquisitions and investments, see "— Acquisitions and Investments."

Sanctions Programs

We have a program designed to comply with applicable economic and trade sanctions programs, including those administered and enforced by the U.S. Department of the Treasury's Office of Foreign Assets Control. These sanctions are usually targeted against foreign countries, terrorists, international narcotics traffickers and those believed to be involved in the proliferation of weapons of mass destruction. These regulations generally require either the blocking of accounts or other property of specified entities or individuals, but they may also require the rejection of certain transactions involving specified entities or individuals. We maintain policies, procedures and other internal controls designed to comply with these sanctions programs.

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Executive Officers of the Registrant

Set forth below is information concerning our executive officers, each of whom is a member of our Executive Committee.

Name	Age	Position
David W. Nelms	54	Chairman and Chief Executive Officer
Roger C. Hochschild	50	President and Chief Operating Officer
R. Mark Graf	50	Executive Vice President and Chief Financial Officer
Kathryn McNamara Corley	55	Executive Vice President, General Counsel and Secretary
Steven E. Cunningham	45	Senior Vice President and Chief Risk Officer
Carlos M. Minetti	52	Executive Vice President and President - Consumer Banking
Diane E. Offereins	57	Executive Vice President and President - Payment Services
James V. Panzarino	62	Executive Vice President and President - Credit and Card Operations
R. Douglas Rose	46	Senior Vice President and Chief Human Resources Officer
Glenn P. Schneider	53	Executive Vice President and Chief Information Officer
Harit Talwar	54	Executive Vice President and President - U.S. Cards

David W. Nelms is our Chairman and Chief Executive Officer. He has held the role of Chief Executive Officer since February 2004 and assumed the role of Chairman in January 2009. Mr. Nelms served as President and Chief Operating Officer from 1998 to 2004. Prior to joining us, Mr. Nelms worked at MBNA America Bank from 1990 to 1998, most recently as Vice Chairman. Mr. Nelms holds a Bachelor's degree in Mechanical Engineering from the University of Florida and an M.B.A. from Harvard Business School.

Roger C. Hochschild is our President and Chief Operating Officer. He has held this role since March 2004. Mr. Hochschild was Executive Vice President, Chief Administrative Officer and Chief Strategic Officer (2001 to 2004) and Executive Vice President, Chief Marketing Officer (1998 to 2001) of our former parent company Morgan Stanley. Mr. Hochschild holds a Bachelor's degree in Economics from Georgetown University and an M.B.A. from the Amos Tuck School at Dartmouth College.

R. Mark Graf is our Executive Vice President and Chief Financial Officer. He has held this role since April 2011. He was also Chief Accounting Officer until December 2012. Prior to joining us, Mr. Graf was an investment advisor with Aquiline Capital Partners, a private equity firm specializing in investments in the financial services industry. From 2006 to 2008, Mr. Graf was a partner at Barrett Ellman Stoddard Capital. Mr. Graf was Executive Vice President and Chief Financial Officer for Fifth Third Bank from 2004 to 2006, after having served as its Treasurer from 2001 to 2004. He holds a Bachelor's degree in Economics from the Wharton School of the University of Pennsylvania.

Kathryn McNamara Corley is our Executive Vice President, General Counsel and Secretary. She has held this role since February 2008. Previously, she served as Senior Vice President, General Counsel and Secretary (1999 to 2008). Prior to becoming General Counsel, Ms. Corley was Managing Director for our former parent company Morgan Stanley's global government and regulatory relations. Ms. Corley holds a Bachelor's degree in Political Science from the University of Southern California and a J.D. from George Mason University School of Law.

Steven E. Cunningham is our Senior Vice President and Chief Risk Officer. He has held this role since May 2013. In his role, he is also responsible for the Comprehensive Capital Analysis and Review and Resolution Planning program offices. Previously, he served as Senior Vice President and Treasurer (2010 to 2013). Prior to joining us, Mr. Cunningham was the Chief Financial Officer for Harley Davidson Financial Services from 2009 to 2010. From 2000 to 2009, he served in several financial and treasury roles with Capital One Financial, including Chief Financial Officer of our banking and auto finance segments. From 1991 to 2000, Mr. Cunningham held numerous roles with the FDIC in the Atlanta and Washington, D.C. offices. He holds a Bachelor's degree in Finance from the University of Alabama and a M.B.A. from The George Washington University.

Carlos Minetti is our Executive Vice President and President - Consumer Banking. He has held this role since February 2014. Previously, he served as Executive Vice President, President - Consumer Banking and Operations (2010

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to 2014), Executive Vice President, Cardmember Services and Consumer Banking (2006 to 2010), and Executive Vice President, and Chief Risk Officer for Cardmember Services and Risk Management (2001 to 2006). Prior to joining us, Mr. Minetti worked in card operations and risk management for American Express from 1987 to 2000, most recently as Senior Vice President. Mr. Minetti holds a Bachelor's degree in Industrial Engineering from Texas A & M University and an M.B.A. from the University of Chicago.

Diane E. Offereins is our Executive Vice President and President - Payment Services. She has held this role since April 2010. Previously, she served as Executive Vice President, Payment Services (2008 to 2010) and Executive Vice President and Chief Technology Officer (1998 to 2010). In 2006, she assumed leadership of the PULSE network. Prior to joining us, Ms. Offereins worked at MBNA America Bank from 1993 to 1998, most recently as Senior Executive Vice President. Ms. Offereins holds a Bachelor's degree in Accounting from Loyola University.

James V. Panzarino is our Executive Vice President and President - Credit and Card Operations. He has held this role since December 2014. Previously, he served as Executive Vice President and Chief Credit and Card Operations Officer (2014), Executive Vice President and Chief Credit Risk Officer (2009 to 2013), Senior Vice President and Chief Credit Risk Officer (2006 to 2009), and Senior Vice President, Cardmember Assistance (2003 to 2006). Prior to joining us, Mr. Panzarino was Vice President of External Collections and Recovery at American Express from 1998 to 2002. Mr. Panzarino holds a Bachelor's degree in Business Management and Communication from Adelphi University.

R. Douglas Rose is our Senior Vice President and Chief Human Resources Officer. He has held this role since April 2013. Prior to joining us, he served as Vice President, Human Resources at United Airlines from 2009 to 2013. He was also Senior Vice President, Human Resources at Capital One and a Human Resources consultant for Hewitt Associates. Mr. Rose holds a Bachelor's degree in Communications from the University of Pennsylvania and a Master's degree from the University of Michigan.

Glenn P. Schneider is our Executive Vice President and Chief Information Officer. He has held this role since January 2015. Previously, he served as Senior Vice President and Chief Information Officer (2008 to 2015), Senior Vice President, Application Development (2003 to 2008), and Vice President, Marketing Applications (1998 to 2003). Prior to joining us in 1993, Mr. Schneider worked for Kemper Financial Services as a Programmer. He holds a Bachelor's degree in Economics/Computer Science with a minor in Statistics from Northern Illinois University.

Harit Talwar is our Executive Vice President and President - U.S. Cards. He has held this role since April 2010. Previously, he served as Executive Vice President, Card Programs and Chief Marketing Officer (2008 to 2010), Executive Vice President, Discover Network (2003 to 2008), and Managing Director for our international business (2000 to 2003). Prior to joining us, Mr. Talwar held a number of positions at Citigroup from 1985 to 2000, most recently as Country Head, Consumer Banking Division, Poland. Mr. Talwar holds a B.A. (Hons) degree in Economics from Delhi University in India and an M.B.A. from the Indian Institute of Management, Ahmedabad.

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Item 1A. Risk Factors

You should carefully consider each of the following risks described below and all of the other information in this annual report on Form 10-K in evaluating us. Our business, financial condition, cash flows and/or results of operations could be materially adversely affected by any of these risks. The trading price of our common stock could decline due to any of these risks. This annual report on Form 10-K also contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including the risks faced by us described below and elsewhere in this annual report on Form 10-K. See “Special Note Regarding Forward-Looking Statements,” which immediately follows the risks below.

Current Economic and Regulatory Environment

Economic conditions have had and could have a material adverse effect on our business, results of operations and financial condition.

As a provider of consumer financial services, our business, results of operations and financial condition are subject to the United States and global economic environment. Although the economy has continued to improve generally with respect to employment and housing market conditions, the improvement has not been at a rapid pace. A customer's ability and willingness to repay us can be negatively impacted by economic conditions and other payment obligations. We are experiencing a period of historical lows in our delinquency and charge-off rates and we expect that these rates will be increasing over time. The over 30 days delinquency rate for total loan receivables was 1.66% at December 31, 2014, up from 1.64% at December 31, 2013. The full-year net charge-off rate for total loan receivables was 2.04% for the year ended December 31, 2014, up from 1.98% for the year ended December 31, 2013. We expect increases in our allowance for loan losses in 2015, which will negatively impact our net income.

Economic conditions also can reduce the usage of credit cards in general and the average purchase amount of transactions industry-wide, including our cards, which reduces interest income and transaction fees. We rely heavily on interest income from our credit card business to generate earnings. Our interest income from credit card loans was $6.4 billion for the year ended December 31, 2014, which was 75% of revenues (defined as interest income plus other income), compared to $6.0 billion for the year ended December 31, 2013, which was 73% of revenues. Economic conditions combined with a competitive marketplace could result in Discover being unable to grow loans, resulting in reduced revenue from its core direct banking business.

Financial regulatory reform initiatives have and will continue to significantly impact the regulatory environment for the financial services industry, which could adversely impact our business, results of operations and financial condition.

The Dodd-Frank Act contains comprehensive provisions governing the practices and oversight of financial institutions and other participants in the financial markets. The Dodd-Frank Act regulates large systemically significant financial firms, including Discover, through a variety of measures, including increased capital and liquidity requirements, limits on leverage and enhanced supervisory authority. Federal banking regulators have issued and continue to propose new regulations and supervisory guidance under the Dodd-Frank Act and otherwise, and have been increasing their examination and enforcement activities. We expect regulators to continue addressing concerns through formal enforcement actions against financial institutions or non-public supervisory actions or findings.

The impact of the evolving regulatory environment on our business and operations depends upon a number of factors including the supervisory priorities and actions of the Federal Reserve, the FDIC and the CFPB, the actions of our competitors and other marketplace participants, and the behavior of consumers. Regulatory developments, findings and ratings could negatively impact our business strategies or require us to: limit or change our business practices, restructure our products in ways that we may not currently anticipate, limit our product offerings, invest more management time and resources in compliance efforts, limit the fees we can charge for services, or limit our ability to pursue certain business opportunities and obtain related required regulatory approvals. For additional information regarding bank regulatory limitations on acquisitions and investments, see "Business — Supervision and Regulation — Acquisitions and Investments." See Note 19: Litigation and Regulatory Matters to our consolidated financial statements for more information on recent matters affecting Discover. Regulatory developments could also impact our

strategies, the value of our assets, or otherwise adversely affect our businesses.

Compliance expenditures have increased significantly for Discover and other financial services firms, and we expect them to continue to increase as regulators remain focused on controls and operational processes. We may face

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additional compliance and regulatory risk to the extent that we enter into new business arrangements with third-party service providers, alternative payment providers or other industry participants. The additional expense, time and resources needed to comply with ongoing regulatory requirements may adversely impact our business and results of operations.

For more information regarding the regulatory environment and developments potentially impacting Discover, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments."

Strategic Business Risk

We face competition in the credit card market from other consumer financial services providers, and we may not be able to compete effectively, which could result in fewer customers and lower account balances and could materially adversely affect our financial condition, cash flows and results of operations.

The consumer financial services business is highly competitive. We compete with other consumer financial services providers on the basis of a number of factors, including brand, reputation, customer service, product offerings, incentives, pricing and other terms. Competition in credit cards is also based on merchant acceptance and the value provided to the customer by rewards programs. Many credit card issuers have instituted rewards programs that are similar to ours, and, in some cases, are more attractive to customers than our programs. These competitive factors affect our ability to attract and retain customers, increase usage of our products and maximize the revenue generated by our products. In addition, because most domestically-issued credit cards, other than those issued by American Express, are issued on the Visa and MasterCard networks, most other card issuers benefit from the dominant position and marketing and pricing power of Visa and MasterCard. The competitive marketplace, combined with slow economic growth, could result in Discover being unable to grow loans, resulting in reduced revenue from its core direct banking business. If we are unable to compete successfully, or if competing successfully requires us to take aggressive actions in response to competitors' actions, our financial condition, cash flows and results of operations could be materially adversely affected.

We incur considerable expenses in competing with other consumer financial services providers, and many of our competitors have greater financial resources than we do, which may place us at a competitive disadvantage and negatively affect our financial results.

We incur considerable expenses in competing with other consumer financial services providers to attract and retain customers and increase usage of our products. A substantial portion of these expenses relates to marketing expenditures. We incurred expenses of $735 million and $717 million for the years ended December 31, 2014 and 2013, respectively, for marketing and business development. Our consumer financial services products compete primarily on the basis of pricing, terms and service. Because of the highly competitive nature of the credit card issuing business, a primary method of competition among credit card issuers, including us, has been to offer rewards programs, low introductory interest rates, attractive standard purchase rates and balance transfer programs that offer a favorable annual percentage rate or other financial incentives for a specified length of time on account balances transferred from another credit card. In the fourth quarter of 2014, we incurred a $178 million charge to earnings to enhance our rewards program by allowing easier redemption of rewards, which resulted in the elimination of our current estimate of customer rewards forfeiture, a contra-liability account.

Competition is intense in the credit card industry, and customers may frequently switch credit cards or transfer their balances to another card. We expect to continue to invest in initiatives to remain competitive in the consumer financial services industry, including the launch of new cards and features, brand awareness initiatives, targeted marketing, online and mobile enhancements, e-wallet participation, customer service improvements, credit risk management and operations enhancements, and infrastructure efficiencies. There can be no assurance that any of the expenses we incur or incentives we offer to attempt to acquire and maintain accounts and increase usage of our products will be effective. In addition, to the extent that we offer new products, features or services to remain competitive, we may be subject to increased operational or other risks.

Furthermore, many of our competitors are larger than we are, have greater financial resources than we do, have more breadth in consumer banking products, and/or have lower funding and operating costs than we have and expect to

have, and have assets such as branch locations and co-brand relationships, that may be appealing to certain customers. For example, larger credit card issuers, which have greater resources than we do, may be better positioned to fund appealing rewards, marketing and advertising programs. We may be at a competitive disadvantage as a result of the greater financial resources, diversification and scale of many of our competitors.

Our expenses directly affect our earnings results. Many factors can influence the amount of our expenses, as well as how quickly they may increase. Our ongoing investments in infrastructure, which may be necessary to maintain a competitive business, integrate newly-acquired businesses, and establish scalable operations, increase our expenses. In addition, as our business develops, changes or expands, additional expenses can arise as a result of a reevaluation of business strategies, management of outsourced services, asset purchases, structural reorganization, compliance with new laws or regulations or the integration of newly-acquired businesses. If we are unable to successfully manage our expenses, our financial results will be negatively affected.

We face competition from other operators of payment networks and alternative payment providers, and we may not be able to compete effectively, which could result in reduced transaction volume, limited merchant acceptance of our cards, limited issuance of cards on our networks by third parties and materially reduced earnings from our payment services business.

We face substantial and increasingly intense competition in the payments industry, both from traditional players and new, emerging alternative payment providers. For example, we compete with other payment networks to attract network partners to issue credit and debit cards and other card products on the Discover, PULSE and Diners Club networks. Competition with other operators of payment networks is generally based on issuer fees, fees paid to networks (including switch fees), merchant acceptance, network functionality and other economic terms. Competition is also based on customer perception of service quality, brand image, reputation and market share. Further, we are facing increased competition from alternative payment providers, who may create innovative network arrangements with our primary competitors or other industry participants, which could adversely impact our costs, transaction volume and ability to grow our business.

Many of our competitors are well established, larger than we are and/or have greater financial resources than we do. These competitors have provided financial incentives to card issuers, such as large cash signing bonuses for new programs, funding for and sponsorship of marketing programs and other bonuses. Visa and MasterCard each enjoy greater merchant acceptance and broader global brand recognition than we do. Although we have made progress in merchant acceptance, we have not achieved global market parity with Visa and MasterCard. In addition, Visa and MasterCard have entered into long-term arrangements with many financial institutions that may have the effect of discouraging those institutions from issuing credit cards on the Discover Network or issuing debit cards on the PULSE network. Some of these arrangements are exclusive, or nearly exclusive, which further limits our ability to conduct material amounts of business with these institutions. If we are unable to remain competitive on issuer fees and other incentives, we may be unable to offer adequate pricing to network partners while maintaining sufficient net revenues.

We also face competition as merchants put pressure on transaction fees. Increasing merchant fees or acquirer fees could adversely affect our effort to increase merchant acceptance of credit cards issued on the Discover Network and may cause merchant acceptance to decrease. This, in turn, could adversely affect our ability to attract network partners and our ability to maintain or grow revenues from our proprietary network. In addition, competitor's settlements with merchants and related actions, including pricing pressures and/or surcharging, could negatively impact our business practices. In response to the Dodd-Frank Act, competitor actions related to the structure of merchant and acquirer fees and merchant and acquirer transaction routing strategies have adversely affected and are expected to continue to adversely affect our PULSE network's business practices, network transaction volume, revenue and prospects for future growth, and entry into new product markets. Visa has entered into arrangements with some merchants and acquirers that has, and is expected to continue to have, the effect of discouraging those merchants and acquirers from routing debit transactions to PULSE. In addition, the Dodd-Frank Act's network participation requirements and competitor actions negatively impact PULSE’s ability to enter into exclusivity arrangements, which affects PULSE’s current business practices and may materially adversely affect its network transaction volume and revenue. PULSE filed a lawsuit against Visa in late 2014 with respect to these competitive concerns, which will significantly impact expenses for the payment services segment. PULSE’s transaction processing revenue was $182 million and $192 million for the years ended December 31, 2014 and 2013, respectively.

American Express is also a strong competitor, with international acceptance, high transaction fees and an upscale brand image. Internationally, American Express competes in the same market segments as Diners Club. We may face challenges in increasing international acceptance on our networks, particularly if third parties that we rely on to issue

Diners Club cards, increase card acceptance and market our brands do not perform to our expectations.
In addition, if we are unable to maintain sufficient network functionality to be competitive with other networks, or if our competitors develop better data security solutions or more innovative products and services than we do, our ability to retain and attract network partners and maintain or increase the revenues generated by our proprietary card

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issuing business or our PULSE business may be materially adversely affected. Additionally, competitors may develop data security solutions which, as a consequence of the competitors' market power, we may be forced to use. As a result, those competitors could subject us to adverse restrictions and our business may be adversely affected.

Our business depends upon relationships with issuers, merchant acquirers and licensees, which are generally financial institutions. The economic and regulatory environment and increased consolidation in the financial services industry decrease our opportunities for new business and may result in the termination of existing business relationships if a business partner is acquired or goes out of business. In addition, as a result of this environment, financial institutions may have decreased interest in engaging in new card issuance opportunities or expanding existing card issuance relationships, which would inhibit our ability to grow our payment services business. We continue to face substantial and intense competition in the payments industry, which impacts our revenue margins, transaction volume and business strategies. Transaction processing volume declined in the third and fourth quarters due to a third-party issuer contract related to our network partner business that was not renewed in 2014. Although this loss of volume was mostly complete at the end of 2014, and we have added volume with our business-to-business payments arrangement, the added volume is lower margin. Also, as previously disclosed, we expect to lose significant volume from a large PULSE debit issuer beginning in 2015. The loss of these volumes significantly impacts our payment services volume and profits, but does not impact our overall profitability.

If we are unsuccessful in maintaining our international network business and achieving meaningful global card acceptance, we may be unable to grow our international network business.

We have made progress toward, but have not completed, achieving global card acceptance across the Diners Club network, the Discover Network and PULSE since we acquired the Diners Club network and related assets in 2008. This would allow Discover customers to use their cards at merchant and ATM locations that accept Diners Club cards around the world and would allow Diners Club customers to use their cards on the Discover Network in North America and on the PULSE network both domestically and internationally.

Our international network business depends upon the cooperation, support and continuous operation of the network licensees that issue Diners Club cards and that maintain a merchant acceptance network. As is the case for other card payment networks, our Diners Club network does not issue cards or determine the terms and conditions of cards issued by the network licensees, with the exception of the Diners Club Italy issuing business, which we acquired in 2013. If we are unable to continue our relationships with network licensees or if the network licensees are unable to continue their relationships with merchants, our ability to maintain or increase revenues and to remain competitive would be adversely affected due to the potential deterioration in customer relationships and related demand that could result. Further, if one or more licensees were to experience a significant impairment of their business or were to cease doing business for economic, regulatory or other reasons, we would face the adverse effects of business interruption in a particular market, including loss of volume, acceptance and revenue, and exposure to potential reputational risk. Such conditions resulted in our acquisition of Diners Club Italy and financial assistance to our Slovenian licensee, resulting in a charge to earnings of approximately $40 million in the second quarter of 2013. In the fourth quarter of 2014, we classified Diners Club Italy as held-for-sale, which resulted in an additional charge to earnings of approximately $21 million. Our ability to sell Diners Club Italy is subject to uncertainty and complexity. Further, Citigroup continues to own and operate network licensees generating a large share of the Diners Club network sales volume. In 2014, Citigroup announced the potential sale of Diners Club Japan, the largest licensee in both volume and revenue. In addition, other Diners Club licensees around the world face challenges as well. When these events occur, we may deploy resources and incur expenses to support various transition activities in order to sustain network acceptance. Interruption of network licensee relationships could have an adverse effect on the acceptance of Discover cards when they are used on the Diners Club network outside of North America.

Also, as we have non-amortizable intangible assets that resulted from the purchase of Diners Club, if we are unable to maintain or increase revenues due to the reasons described above, we may be exposed to an impairment loss on the Diners Club acquisition that, when recognized, could have a material adverse impact on our consolidated financial condition and results of operations. The long-term success of our international network business depends upon achieving meaningful global card acceptance, which has included and may continue to include higher overall costs or longer timeframes than anticipated.

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The success of our student loan strategy depends upon our ability to manage the risks of our student loan portfolio and the student lending environment. If we fail to do so, we may be unable to sustain and grow our student loan portfolio.
Our private student loan portfolio has grown from $1.0 billion at November 30, 2010 to $8.5 billion at December 31, 2014. The long-term success of our student loan strategy depends upon our ability to manage the credit risk, pricing, funding, operations and expenses of a larger student loan portfolio, as well as grow student loan originations. Our student loan strategy is also impacted by external factors such as the overall economic environment, a challenging regulatory environment for private student loans and a competitive marketplace. For more information on the regulatory environment, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments — Consumer Financial Services — Private Student Loans" and Note 19: Litigation and Regulatory Matters to our consolidated financial statements. Slow economic recovery combined with government and regulatory focus on student lending and competitive factors, such as the need to offer fixed interest rates, may present challenges to managing and growing our private student loan business in the future, and could cause us to restructure our private student loan product in ways that we may not currently anticipate. In addition, changes that adversely affect the private student loan market generally may negatively impact the profitability and growth of our student loan portfolio.
The success of our home loans strategy depends upon our ability to market, originate and sell mortgage loans. If we are unable to do so, our long-term strategy and overall success will be adversely affected.
The success of our home loans strategy depends upon our ability to generate mortgage loan origination volume. Our origination volume is largely dependent on our ability to offer competitively priced, desirable loan products under the Discover brand and our ability to attract qualified prospective borrowers. Our origination volumes are also affected by certain external factors outside our control, including adverse economic conditions and reductions in refinance volumes. This has put pressure on us to develop our purchase mortgage capability to replace some of the lost refinance loan volume. Historically, direct-to-consumer businesses have been more successful in the refinance business and less successful in the purchase market, and we face challenges in developing a scalable direct-to-consumer purchase mortgage origination business. Overall economic conditions as well as an inability to attract customers in the purchase market has led and may continue to lead to fewer loan originations than expected, which adversely affects our ability to grow the business and results in reduced earnings. In the fourth quarter of 2014, our lack of progress in meeting these challenges resulted in an approximately $27 million charge to earnings related to the impairment of goodwill realized with the acquisition of our mortgage origination platform. We will continue to evaluate our home loans strategy.
Our success also depends upon relationships with financial intermediaries, including secondary market purchasers, to which we sell eligible mortgages on a servicing-released basis, and our warehouse lender, which provides funding from the time we fund a customer's mortgage until it is sold to a secondary market purchaser. The secondary mortgage market, as well as the availability of mortgage financing, has experienced disruptions resulting from reduced investor demand and/or increased investor yield requirements for mortgage loans and associated mortgage servicing rights (including the government-sponsored enterprises Fannie Mae and Freddie Mac) and mortgage-backed securities. Most of the market liquidity in the mortgage industry is provided, either directly or indirectly, by government sponsored entities or government agencies. Any attempts to shift market liquidity to private capital sources could impose risk to the mortgage industry to the extent that changes reduce the capacity of available funding. If we are unable to sell our loans in the secondary market, sell servicing, or retain our warehouse facility, we could incur additional credit risk and losses, and funding costs and liquidity could be adversely impacted.
The long-term success of our home loans strategy depends partly upon our ability to manage the expenses and risks of offering home loan products. If we cannot execute a successful strategy, we may continue to experience losses in this area. In addition, we may incur additional expenses and risks if we are unable to successfully address and manage regulatory, counterparty and industry-related risks.
We may experience unanticipated losses as a result of mortgage loan repurchase and indemnification obligations under agreements with secondary market purchasers.
We may be required to repurchase mortgage loans that have been sold to secondary market purchasers in the event there are breaches of certain representations and warranties contained within the sales agreements, such as improper

underwriting, fraud, or other origination defects. We also may be required to indemnify certain purchasers and others against losses they incur in the event of breaches of representations and warranties and in various other circumstances, and the amount of such losses could exceed the repurchase amount of the related loans. In connection

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with the sale of loans to certain secondary market purchasers, we also expect to refund premiums paid by secondary market purchasers in instances where the borrower prepays the loan within a specified period of time. We would need to find alternative purchasers for, or arrange with a third party to service, any loans that we are unable to sell or are required to repurchase.

Consequently, we are exposed to credit risk, and potentially funding risk, associated with sold loans due to the risk we may be required to repurchase these loans. We establish reserves in our consolidated financial statements for potential losses related to the risk of having to repurchase mortgage loans we have sold. The adequacy of the reserves and the ultimate amount of losses incurred will depend on, among other things, the actual future mortgage loan performance, the actual level of future repurchase and indemnification requests, the actual success rate of claimants, actual recoveries on the collateral and macroeconomic conditions. Due to continued uncertainties relating to the credit performance of mortgages, the reserves we establish may not be adequate and losses incurred could adversely affect our financial condition and results of operations.

Acquisitions or strategic investments that we pursue may not be successful and could disrupt our business, harm our financial condition or reduce our earnings.

In the past few years, Discover has been expanding its business beyond credit cards, both organically and through acquisitions. We may consider or undertake additional strategic acquisitions of, or material investments in, businesses, products, portfolios of loans or technologies in the future. We may not be able to identify suitable acquisition or investment candidates, or even if we do identify suitable candidates, they may be difficult to finance, expensive to fund and there is no guarantee that we can obtain any necessary regulatory approvals or complete the transactions on terms that are favorable to us. We generally must receive federal regulatory approvals before we can acquire a bank, bank holding company, deposits or certain assets or businesses. For additional information regarding bank regulatory limitations on acquisitions and investments, see "Business — Supervision and Regulation — Acquisitions and Investments."

To the extent we pay the purchase price of any acquisition or investment in cash, it may have an adverse effect on our financial condition; similarly, if the purchase price is paid with our stock, it may be dilutive to our stockholders. In addition, we may assume liabilities associated with a business acquisition or investment, including unrecorded liabilities that are not discovered at the time of the transaction, and the repayment or settlement of those liabilities may have an adverse effect on our financial condition.

We may not be able to successfully integrate the personnel, operations, businesses, products, or technologies of an acquisition or investment. Integration may be particularly challenging if we enter into a line of business in which we have limited experience and the business operates in a difficult legal, regulatory or competitive environment. We may find that we do not have adequate operations or expertise to manage the new business. The integration of any acquisition or investment may divert management's time and resources from our core business, which could impair our relationships with our current employees, customers and strategic partners and disrupt our operations.

Acquisitions and investments also may not perform to our expectations for various reasons, including the loss of key personnel, customers or vendors. If we fail to integrate acquisitions or investments or realize the expected benefits, we may lose the return on these acquisitions or investments or incur additional transaction costs, and our business, reputation and financial condition may be harmed as a result.

Credit, Market and Liquidity Risk

Our business depends on our ability to manage our credit risk, and failing to manage this risk successfully may result in high charge-off rates, which would materially adversely affect our business, profitability and financial condition.

We seek to grow our loan receivables while maintaining quality credit performance. Our success depends on our ability to manage our credit risk while attracting new customers with profitable usage patterns. We select our customers, manage their accounts and establish terms and credit limits using proprietary scoring models and other analytical techniques that are designed to set terms and credit limits to appropriately compensate us for the credit risk we accept, while encouraging customers to use their available credit. The models and approaches we use may not accurately predict future charge-offs due to, among other things, inaccurate assumptions. While we continually seek to improve our assumptions and models, we may make modifications that unintentionally cause them to be less predictive or we may incorrectly interpret the data produced by these models in setting our credit policies.

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Our ability to manage credit risk and avoid high charge-off rates may be adversely affected by economic conditions that may be difficult to predict as explained in our economic conditions risk factor at the beginning of this section. The full-year net charge-off rate for total loan receivables was 2.04% in 2014, up from 1.98% in 2013. At December 31, 2014 and 2013, $660 million, or 0.94%, and $634 million, or 0.96%, of our loan receivables were non-performing (defined as loans over 90 days delinquent and accruing interest plus loans not accruing interest). We are experiencing a period of historical lows in our delinquency and charge-off rates and we expect that these rates will be increasing over time. There can be no assurance that our underwriting and portfolio management strategies will permit us to avoid high charge-off levels, or that our allowance for loan losses will be sufficient to cover actual losses.

A customer's ability and willingness to repay us can be negatively impacted by increases in their payment obligations to other lenders and by restricted availability of credit to consumers generally. Our collection operations may not compete effectively to secure more of customers' diminished cash flow than our competitors. In addition, we may fail to quickly identify customers who are likely to default on their payment obligations and reduce our exposure by closing credit lines and restricting authorizations, which could adversely impact our financial condition and results of operations. Our ability to manage credit risk also may be adversely affected by legal or regulatory changes (such as restrictions on collections, bankruptcy laws, minimum payment regulations and re-age guidance), competitors' actions and consumer behavior, as well as inadequate collections staffing, techniques and models.

We continue to expand our marketing of our personal, private student loan and home loan products, including the launch of a new home equity loan product in late 2013. We have less experience in these areas as compared to our traditional credit card lending business, and there can be no assurance that we will be able to grow these products in accordance with our strategies, manage our credit and other risks associated with these products, or generate sufficient revenue to cover our expenses in these markets. Our failure to manage our credit and other risks may materially adversely affect our profitability and our ability to grow these products, limiting our ability to further diversify our business.

Adverse market conditions or an inability to effectively manage our liquidity risk could negatively impact our ability to meet our liquidity and funding needs, which could materially adversely impact our business operations and overall financial condition.

We must effectively manage the liquidity risk to which we are exposed. We require liquidity in order to meet cash requirements such as day-to-day operating expenses, extensions of credit on our consumer loans and required payments of principal and interest on our borrowings. Our primary sources of liquidity and funding are payments on our loan receivables, deposits, and proceeds from securitization transactions and securities offerings. We may maintain too much liquidity, which can be costly and limit financial flexibility, or we may be too illiquid, which could result in financial distress during a liquidity stress event. Our liquidity portfolio had a balance of approximately $10.8 billion as of December 31, 2014, compared to $11.1 billion as of December 31, 2013. Our total contingent liquidity sources as of December 31, 2014 amounted to $34.3 billion (consisting of $10.8 billion in our liquidity portfolio, $16.0 billion in incremental Federal Reserve discount window capacity, and $7.5 billion of undrawn capacity in private securitizations), compared to $32.6 billion at December 31, 2013.

In the event that our current sources of liquidity do not satisfy our needs, we would be required to seek additional financing. The availability of additional financing will depend on a variety of factors such as market conditions, the general availability of credit to the financial services industry, new regulatory restrictions and requirements, and our credit ratings. Disruptions, uncertainty or volatility in the capital, credit or deposit markets, such as the volatility experienced in the capital and credit markets during the financial crisis of 2007, may limit our ability to repay or replace maturing liabilities in a timely manner. As such, we may be forced to delay raising funding or be forced to issue or raise funding at undesirable terms and/or costs, which could decrease profitability and significantly reduce financial flexibility. Regulations such as the liquidity coverage ratio (LCR), as part of the Basel III accord, may increase the cost of funding and impact funding availability and are described more fully in "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments." Further, in disorderly financial markets or for other reasons, it may be difficult or impossible to liquidate some of our investments to meet our liquidity needs.

While market conditions have stabilized and, in many cases, improved, there can be no assurance that significant disruption and volatility in the financial markets will not occur in the future. Likewise, adverse developments with respect to financial institutions and other third parties with whom we maintain important financial relationships could negatively impact our funding and liquidity. If we are unable to continue to fund our assets through deposits or access capital markets on favorable terms, or if we experience an increase in our borrowing costs or otherwise fail to

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manage our liquidity effectively, our liquidity, operating results, financial results and condition may be materially adversely affected.

An inability to accept or maintain deposits in the future could materially adversely affect our liquidity position and our ability to fund our business.

We obtain deposits from consumers either directly or through affinity relationships and through third-party securities brokerage firms that offer our deposits to their customers. We had $28.8 billion in deposits acquired directly or through affinity relationships and $17.3 billion in deposits originated through securities brokerage firms as of December 31, 2014, compared to $28.4 billion and $16.4 billion, respectively, as of December 31, 2013. Competition from other financial services firms that use deposit funding and the rates and services we offer on our deposit products may affect deposit renewal rates, costs or availability. Changes we make to the rates offered on our deposit products may affect our profitability (through funding costs) and our liquidity (through volumes raised). In addition, our ability to maintain existing or obtain additional deposits may be impacted by factors, including factors beyond our control, such as: perceptions about our financial strength; quality of deposit servicing or online banking generally, which could reduce the number of consumers choosing to make deposits with us; third parties continuing or entering into affinity relationships with us; or third-party securities brokerage firms offering our deposit products.

Our ability to obtain deposit funding and offer competitive interest rates on deposits is also dependent on capital levels of our bank subsidiaries. The FDIA in certain circumstances prohibits insured banks, such as our subsidiary Discover Bank, from accepting brokered deposits (as defined in the FDIA) and applies other restrictions, such as a cap on interest rates we may pay. See “Business — Supervision and Regulation” and Note 17: Capital Adequacy to our consolidated financial statements for more information. As of December 31, 2014, we had brokered deposits (as defined in the FDIA) of $17.3 billion. While Discover Bank met the FDIC's definition of “well-capitalized” as of December 31, 2014, and has no restrictions regarding acceptance of brokered deposits or setting of interest rates, there can be no assurance that it will continue to meet this definition. Additionally, our regulators can adjust the requirements to be "well-capitalized" at any time and have authority to place limitations on our deposit businesses, including the interest rate we pay on deposits.

If we are unable to securitize our receivables, it may have a material adverse effect on our liquidity, cost of funds and overall financial condition.

We use the securitization of credit card receivables, which involves the transfer of receivables to a trust and the issuance by the trust of beneficial interests to third-party investors, as a significant source of funding as well as for contingent liquidity. Our average level of credit card securitized borrowings from third parties was $15.1 billion and $14.3 billion for the years ended December 31, 2014 and 2013, respectively. Although the securitization market for credit cards has been re-established since the financial crisis, there can be no assurance that there will not be future disruptions in the market. Our ability to raise funding through the securitization market also depends, in part, on the credit ratings of the securities we issue from our securitization trusts. If we are not able to satisfy rating agency requirements to maintain the ratings of asset-backed securities issued by our trusts, it could limit our ability to access the securitization markets. Additional factors affecting the extent to which we may securitize our credit card receivables in the future include the overall credit quality of our receivables, the costs of securitizing our receivables, and the legal, regulatory, accounting and tax requirements governing securitization transactions. For example, the Basel Committee on Banking Supervision recently proposed changes to the rules for banks’ calculation of credit risk capital requirements for exposures to securitization transactions. The timing and impact of these proposed rules are unclear at this time, but they could impact the pricing and/or volume of our asset-backed securities issuances. A prolonged inability to securitize our credit card receivables, or an increase in the costs of such issuances, may have a material adverse effect on our liquidity, cost of funds and overall financial condition.

The occurrence of events that result in the early amortization of our existing credit card securitization transactions or an inability to delay the accumulation of principal collections in our credit card securitization trusts would materially adversely affect our liquidity.

Our liquidity would be materially adversely affected by the occurrence of events that could result in the early amortization of our existing credit card securitization transactions. Our credit card securitizations are structured as “revolving transactions” that do not distribute to securitization investors their share of monthly principal payments

received on the underlying receivables during the revolving period, and instead use those principal payments to fund the purchase of new receivables. The occurrence of an “early amortization event” may result in termination of the revolving periods of our securitization transactions, which would require us to repay the affected outstanding

securitized borrowings out of principal collections without regard to the original payment schedule. Our average level of credit card securitized borrowings from third parties was $15.1 billion and $14.3 billion for the years ended December 31, 2014 and 2013, respectively. Early amortization events include, for example, insufficient cash flows in the securitized pool of receivables to meet contractual requirements (i.e. excess spread less than zero) and certain breaches of representations, warranties or covenants in the agreements relating to the securitization. For more information on excess spread, see Note 5: Credit Card and Student Loan Securitization Activities to our consolidated financial statements. An early amortization event would negatively impact our liquidity, and require us to rely on alternative funding sources, which may or may not be available at the time. An early amortization event also could impact our ability to access the undrawn conduit facilities that we maintain for contingent liquidity purposes.

Our credit card securitization structure includes a requirement that we accumulate principal collections into a restricted account in the amount of scheduled maturities on a pro rata basis over the 12 months prior to a security's maturity date. We have the option under our credit card securitization documents to shorten this accumulation period, subject to the satisfaction of certain conditions, including reaffirmation from each of the rating agencies of the security's required rating. Historically, we have exercised this option to shorten the accumulation period to one month prior to maturity. If we were to determine that the payment rate on the underlying receivables would not support a one-month accumulation period, or if one or more of the rating agencies were to require an accumulation period of longer than one month, we would need to begin accumulating principal cash flows earlier than we have historically. A lengthening of the accumulation period would negatively impact our liquidity, requiring management to implement mitigating measures. During periods of significant maturity levels, absent management actions, the lengthening of the accumulation period could materially adversely affect our financial condition.

A downgrade in the credit ratings of our securities could materially adversely affect our business and financial condition.

We, along with Discover Bank, are regularly evaluated by the ratings agencies, and their ratings for our long-term debt and other securities, including asset-backed securities issued by our securitization trusts, are based on a number of factors that may change from time to time, including our financial strength as well as factors that may not be within our control. Factors that affect our unsecured credit ratings include, but are not limited to, the macroeconomic environment in which we operate and the credit ratings of the U.S. government, the credit quality and performance of our assets, the amount and quality of our capital, the level and stability of our earnings, and the structure and amount of our liquidity. In addition to these factors, the ratings of our asset-backed securities are also based on the quality of the underlying receivables and the credit enhancement structure of the trusts. Downgrades in our ratings or those of our trusts could materially adversely affect our cost of funds, access to capital and funding, and overall financial condition. There can be no assurance that we will be able to maintain our current credit ratings or that our credit ratings will not be lowered or withdrawn.

We may not be successful in managing the investments in our liquidity investment portfolio and investment performance may deteriorate due to market fluctuations, which would adversely affect our business and financial condition.

We must effectively manage the risks of the investments in our liquidity investment portfolio, which is comprised of cash and cash equivalents and high-quality liquid investments. Our liquidity portfolio was $10.8 billion at December 31, 2014. The value of our investments may be adversely affected by market fluctuations including changes in interest rates, prices, prepayment rates, credit risk premiums and overall market liquidity. Also, investments backed by collateral could be adversely impacted by changes in the value of the underlying collateral. In addition, economic conditions may cause certain of the obligors, counterparties and underlying collateral on our investments to incur losses of their own or default on their obligations to us due to bankruptcy, lack of liquidity, operational failure or other reasons, thereby increasing our credit risk exposure to these investments. These risks could result in a decrease in the value of our investments, which could negatively impact our financial condition. These risks could also restrict our access to funding. While the securities in our investment portfolio are currently limited to obligations of high-quality sovereign and government-sponsored issuers, we may choose to expand the range our investments over time, which may result in greater fluctuations in market value. While we expect these investments to be readily convertible into cash and do not believe they present a material increase to our risk profile or will have a material impact on our

risk-based capital ratios, they are subject to certain market fluctuations that may reduce the ability to fully convert them into cash.

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Changes in the level of interest rates could materially adversely affect our earnings.

Changes in interest rates cause our net interest income to increase or decrease, as certain of our assets and liabilities carry interest rates that fluctuate with market benchmarks. External factors may cause interest rates to increase. The inability of the Federal Reserve to adjust monetary policy in a timely manner after a prolonged period of injecting liquidity into the economy as well as other market factors could result in a steep increase in domestic inflation and a resulting need to rapidly increase interest rates. Tighter Federal Reserve monetary policy and rising interest rates would increase the cost of borrowing for consumers, businesses and governments. Higher interest rates could negatively impact Discover's customers as total debt service payments would increase, impede Discover's ability to grow its consumer lending businesses, and increase the cost of funding, which would put Discover at a disadvantage as compared to competitors that have less expensive funding sources.

Some of our consumer loan receivables bear interest at a fixed rate or do not earn interest, and we are not able to increase the rate on those loans to offset any higher cost of funds, which could materially reduce earnings. At the same time, our variable rate loan receivables, which are based on the prime market benchmark rate, may not change at the same rate as our floating-rate borrowings or may be subject to a cap, subjecting us to basis risk. The majority of our floating-rate borrowings and interest rate derivatives are generally based on the one-month LIBOR rate. If the one-month LIBOR rate were to increase without a corresponding increase in the prime rate, our earnings would be negatively impacted. While the majority of our existing certificates of deposit bear interest at fixed rates that do not fluctuate with market benchmarks, we use derivative instruments to hedge the fixed rates associated with some of these certificates of deposit. However, new deposit issuances are subject to fluctuations in interest rates. Moreover, although certificates of deposit we issue directly to consumers are subject to early withdrawal penalties, these penalties may not fully mitigate early withdrawal behavior in a rising interest rate environment.

Interest rates may also adversely impact our delinquency and charge-off rates. Many consumer lending products bear interest rates that fluctuate with certain base lending rates published in the market, such as the prime rate and LIBOR. As a result, higher interest rates often lead to higher payment requirements by consumers under obligations to us and other lenders, which may reduce their ability to remain current on their obligations to us and thereby lead to loan delinquencies and additions to our loan loss provision, which could materially adversely affect our earnings.

We continually monitor interest rates and have a number of tools, including the composition of our investments, liability terms and interest rate derivatives, to manage our interest rate risk exposure. Changes in market assumptions regarding future interest rates could significantly impact our interest rate risk strategy, our financial position and results of operations. If our interest rate risk management strategies are not appropriately monitored or executed, these activities may not effectively mitigate our interest rate sensitivity or have the desired impact on our results of operations or financial condition. For information related to interest rate risk sensitivities, see "Quantitative and Qualitative Disclosures About Market Risk."

We may be limited in our ability to pay dividends on and repurchase our stock.

In the year ended December 31, 2014, we increased our quarterly common stock dividend to $0.24 per share and repurchased approximately 5% of our outstanding common stock under our share repurchase program. The declaration and payment of future dividends, as well as the amount thereof, are subject to the discretion of our board of directors and the Federal Reserve's non-objection to our annual capital plan. The amount and size of any future dividends and share repurchases will depend upon our results of operations, financial condition, capital levels, cash requirements, future prospects, regulatory review and other factors as further described in "Business — Supervision and Regulation — Capital, Dividends and Share Repurchases." Holders of our shares of common stock are subject to the prior dividend rights of holders of our preferred stock or the depositary shares representing such preferred stock outstanding, and if full dividends have not been declared and paid on all outstanding shares of our preferred stock in any dividend period, no dividend may be declared or paid on or set aside for payment on our common stock. Banking laws and regulations and our banking regulators may limit or prohibit our payment of dividends on or our repurchase of our stock at any time. There can be no assurance that we will declare and pay any dividends on or repurchase our stock in the future.

We are a holding company and depend on payments from our subsidiaries.

Discover Financial Services, our parent holding company, depends on dividends, distributions and other payments from its subsidiaries, particularly Discover Bank, to fund dividend payments, share repurchases, payments on its obligations, including debt obligations, and to provide funding and capital as needed to its operating subsidiaries.

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Banking laws and regulations and our banking regulators may limit or prohibit our transfer of funds freely, either to or from our subsidiaries, at any time. These laws, regulations and rules may hinder our ability to access funds that we may need to make payments on our obligations or otherwise achieve strategic objectives. For more information, see "Business — Supervision and Regulation — Capital, Dividends and Share Repurchases."

Operational and Other Risk

Our framework and models for managing risks may not be effective in mitigating our risk of loss.

Our risk management framework seeks to identify and mitigate risk and appropriately balance risk and return. We have established processes and procedures intended to identify, measure, monitor and report the types of risk to which we are subject, including credit risk, market risk, liquidity risk, operational risk, compliance and legal risk, and strategic risk. We seek to monitor and control our risk exposure through a framework of policies, procedures, limits and reporting requirements.

Management of our risks in some cases depends upon the use of analytical and/or forecasting models. We use a variety of models to manage and inform decision making with respect to customers, and for the measurement of risk including credit, market and operational risks and for our finance and treasury functions. Models used by Discover can vary in their complexity and are designed to identify, measure, and mitigate risks at various levels such as loan-level, portfolio segments, entire portfolios and products. These models use a set of computational rules to generate numerical estimates of uncertain values to be used for assessment of price, financial forecasts, and estimates of credit, interest rate, market, and operational risk. All models carry some level of uncertainty that introduces risks in the estimates.

If the models that we use to mitigate risks are inadequate, we may incur increased losses. In addition, there may be risks that exist, or that develop in the future, that we have not appropriately anticipated, identified or mitigated. If our risk management framework and models do not effectively identify or mitigate our risks, we could suffer unexpected losses and our financial condition and results of operations could be materially adversely affected.

If our security systems, or those of third parties, containing information about us, our customers or third parties with which we do business, are compromised, our business could be disrupted and we may be subject to significant financial exposure, liability and damage to our reputation.

Our direct banking and network operations rely heavily on the secure processing, storage and transmission of confidential information about us, our customers and third parties with which we do business. Information security risks for financial institutions have increased and continue to increase in part because of the proliferation of new technologies, the use of the internet, mobile and telecommunications technologies to conduct financial transactions, and the increased sophistication and activities of organized crime, activists, hackers, terrorist organizations, nation state actors and other external parties. Those parties may also attempt to fraudulently induce employees, customers or other users of our systems to disclose sensitive information in order to gain access to our data or that of our customers. Our technologies, systems, networks and software, and those of other financial institutions, have been and are likely to continue to be the target of increasingly frequent cyber-attacks, malicious code, computer viruses, denial of service attacks, social engineering, other remote access attacks, and physical attacks that could result in unauthorized access, misuse, loss or destruction of data (including confidential customer information), account takeovers, unavailability of service or other events. These types of threats may derive from human error, fraud or malice on the part of external or internal parties, or may result from accidental technological failure.

Despite our efforts to ensure the integrity of our systems through our information security and business continuity programs, we may not be able to anticipate or to implement effective preventive measures against all security breaches or events of these types, especially because the techniques used change frequently and quickly or are not recognized until launched, and because:

- Security attacks can originate from a wide variety of sources and geographic locations.
- Because we rely on many third-party service providers and network participants, including merchants, a security breach or cyber-attack affecting one of these third parties could impact us. For example, the financial services industry has seen an increase in point-of-sale breaches at retail merchant locations, which are remote attacks against the environment where retail transactions are authorized (especially card-present purchases), resulting in potential exposure of personal and identifiable information impacting millions of households. For additional information see

the risk factor "— We rely on third parties to deliver services. If

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we face difficulties managing our relationships with third-party service providers, our revenue or results of operations could be materially adversely affected."

- Further, to access our products and services, our customers may use computers and mobile devices that are beyond our security control systems.

We are subject to increasingly more risk related to security systems as we increase acceptance of the Discover card internationally, expand our suite of online direct banking products, enhance our mobile payment technologies, acquire new or outsource some of our business operations, expand our internal usage of web-based products and applications, and otherwise attempt to keep pace with rapid technological changes in the financial services industry. Our efforts to mitigate this risk increase our expenses. While we continue to invest in our cyber security defenses, if our security systems or those of third parties are penetrated or circumvented such that the confidentiality, integrity and availability of information about us, our customers, transactions processed on our networks or third parties with which we do business is compromised, we could be subject to significant liability that may not be covered by insurance, including significant legal and financial exposure, actions by our regulators, damage to our reputation, or a loss of confidence in the security of our systems, products and services that could materially adversely affect our business. For additional information on risks in this area, see the risk factors below regarding fraudulent activity, the introduction of new products and services, the use of third parties for outsourcing, technology generally, and laws and regulations addressing consumer privacy and data use and security.

If we cannot remain organizationally effective, we will be unable to address the opportunities and challenges presented by our strategy and the increasingly dynamic and competitive economic and regulatory environment.

To remain organizationally effective, we must effectively empower, integrate and deploy our management and operational resources and incorporate global and local business, regulatory and consumer perspectives into our decisions and processes. In order to execute on our strategy to be the leading direct bank and payments partner, we must develop and implement innovative and efficient technology solutions and marketing initiatives while effectively managing legal, regulatory, compliance, security, operational and other risks as well as expenses. Examples include the implementation of a broader rollout of our checking product, the expansion of our new core banking platform beyond deposits, a strategy for our home loans platform, and a structure for a more competitive global network business. If we fail to develop and implement these solutions, we may be unable to expand quickly and the results of our expansion may be unsatisfactory. In addition, if we are unable to make decisions quickly, assess our opportunities and risks, execute our strategy, and implement new governance, managerial and organizational processes as needed in this increasingly dynamic and competitive economic and regulatory environment, our financial condition, results of operations, relationships with our business partners, banking regulators, customers and shareholders, and ultimately our prospects for achieving our long-term strategies, may be negatively impacted.

We may be unable to increase or sustain Discover card usage, which could impair growth in, or lead to diminishing, average balances and total revenue.

A key element of our business strategy is to increase the usage of the Discover card by our customers, including making it their primary card, and thereby increase our revenue from transaction and service fees and interest income. However, our customers' use and payment patterns may change because of social, legal and economic factors, and customers may decide to use debit cards or other payment products instead of credit cards, not increase card usage, or pay their balances within the grace period to avoid finance charges. We face challenges from competing card products in our attempts to increase credit card usage by our existing customers. Our ability to increase card usage also is dependent on customer satisfaction, which may be adversely affected by factors outside of our control, including competitors' actions and legislative/regulatory changes. Existing legal and regulatory restrictions limit pricing changes that may impact an account throughout its lifecycle, which may reduce our capability to offer lower price promotions to drive account usage and customer engagement. As part of our strategy to increase usage, we have been increasing the number of merchants who accept cards issued on the Discover Network. If we are unable to continue increasing merchant acceptance or fail to improve awareness of existing merchant acceptance of our cards, our ability to grow usage of Discover cards may be hampered. As a result of these factors, we may be unable to increase or sustain credit card usage, which could impair growth in or lead to diminishing average balances and total revenue.

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Our transaction volume is concentrated among large merchants, and a reduction in the number of large merchants that accept cards on the Discover Network or PULSE network or the rates they pay could materially adversely affect our business, financial condition, results of operations and cash flows.
Discover card transaction volume was concentrated among our top 100 merchants in 2014, with our largest merchant accounting for approximately 8% of that transaction volume. Transaction volume on the PULSE network was also concentrated among the top 100 merchants in 2014, with our largest merchant accounting for approximately 11% of PULSE transaction volume. These merchants could seek to negotiate better pricing or other financial incentives by conditioning their continued participation in the Discover Network and/or PULSE network on a change in the terms of their economic participation. Loss of acceptance at our largest merchants would decrease transaction volume, negatively impact our brand, and could cause customer attrition. In addition, some of our merchants, primarily our remaining small and mid-size merchants, are not contractually committed to us for any period of time and may cease to participate in the Discover Network at any time on short notice.
Actual or perceived limitations on acceptance of credit cards issued on the Discover Network or debit cards issued on the PULSE network could adversely affect the use of Discover cards by existing customers and the attractiveness of the Discover card to prospective customers. Also, we may have difficulty attracting and retaining network partners if we are unable to add or retain acquirers or merchants who accept cards issued on the Discover or PULSE networks. As a result of these factors, a reduction in the number of our merchants or the rates they pay could materially adversely affect our business, financial condition, results of operations and cash flows.
Our business, financial condition and results of operations may be adversely affected by merchants' increasing focus on the fees charged by credit card and debit card networks.
Merchant acceptance and fees are critical to the success of both our card-issuing and payment processing businesses. Merchants are concerned with the fees charged by credit card and debit card networks. They seek to negotiate better pricing or other financial incentives as a condition of continued participation in the Discover Network and PULSE network. During the past few years, merchants and their trade groups have filed numerous lawsuits against Visa, MasterCard, American Express and their card-issuing banks, claiming that their practices toward merchants, including issuer fees, violate federal antitrust laws. There can be no assurance that they will not in the future bring legal proceedings against other credit card and debit card issuers and networks, including us. Merchants also may promote forms of payment with lower fees, such as ACH-based payments, or seek to impose surcharges at the point of sale for use of credit or debit cards. Merchant groups have also promoted federal and state legislation that would restrict issuer practices or enhance the ability of merchants, individually or collectively, to negotiate more favorable fees. The heightened focus by merchants on the fees charged by credit card and debit card networks, together with the Dodd-Frank Act and recent U.S. Department of Justice settlements with Visa and MasterCard, which would allow merchants to encourage customers to use other payment methods or cards and may increase merchant surcharging, could lead to reduced transactions on, or merchant acceptance of, Discover Network or PULSE network cards or reduced fees, any of which could adversely affect our business, financial condition and results of operations.
Political, economic or other instability in a country or geographic region, or other unforeseen or catastrophic events, could adversely affect our international business activities and reduce our revenue.
Natural disasters or other catastrophic events, including terrorist attacks, may have a negative effect on our business and infrastructure, including our information technology systems. Our Diners Club network, concentrated primarily on serving the global travel industry, could be adversely affected by international conditions that may result in a decline in consumer or business travel activity. Armed conflict, public health emergencies, natural disasters or terrorism may have a significant negative effect on travel activity and related revenue. Although a regionalized event or condition may primarily affect one of our network participants, it may also affect our overall network and card activity and our resulting revenue. Overall network and card transaction activity may decline as a result of concerns about safety or disease or may be limited because of economic conditions that result in spending on travel to decline. The impact of such events and other catastrophes on the overall economy may also adversely affect our financial condition or results of operations.
Fraudulent activity associated with our products or our networks could cause our brands to suffer reputational damage, the use of our products to decrease and our fraud losses to be materially adversely affected.

We are subject to the risk of fraudulent activity associated with merchants, customers and other third parties handling customer information. Our fraud losses have been increasing and we incurred losses of $134 million and

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$110 million for the years ended December 31, 2014 and 2013, respectively. Credit and debit card fraud, identity theft and related crimes are prevalent and perpetrators are growing ever more sophisticated. Our resources and fraud prevention tools may be insufficient to accurately predict and prevent fraud. The risk of fraud continues to increase for the financial services industry in general. Additionally, our risk of fraud continues to increase as acceptance of the Discover card grows internationally and we expand our direct banking business. Our financial condition, the level of our fraud charge-offs and other results of operations could be materially adversely affected if fraudulent activity were to significantly increase. High-profile fraudulent activity could negatively impact our brand and reputation. In addition, significant increases in fraudulent activity could lead to regulatory intervention (such as mandatory card reissuance) and reputational and financial damage to our brands, which could negatively impact the use of our cards and networks and thereby have a material adverse effect on our business. Further, fraudulent activity may result in lower license fee revenue from our Diners Club licensees.

The financial services and payment services industries are rapidly evolving, and we may be unsuccessful in introducing new products or services on a large scale in response to these changes.

Technological changes continue to significantly impact the financial services and payment services industries, such as continuing development of technologies in the areas of smart cards, radio frequency and proximity payment devices, electronic commerce and mobile commerce, among others. For example, the industry migration to evolving security (referred to as “EMV”) standards in 2015 will be a fundamental change in how payment transactions are processed and how customers use their cards. There are significant risks in migrating to EMV standards, including merchant acceptance, consumer adoption and technology issues, which may have adverse implications for both our card-issuing and network businesses. The introduction of EMV standards requires changes to our payment systems to permit interoperability among our networks, both domestically and globally. The U.S. payments industry is expected to bring risks and opportunities in 2015 for both our card-issuing and payments businesses in EMV migration as well as increasingly competitive mobile, e-wallet and tokenization solutions.

The effect of technological changes on our business is unpredictable. We depend, in part, on third parties for the development of and access to new technologies. We expect that new services and technologies relating to the payments business will continue to appear in the market, and these new services and technologies may be superior to, or render obsolete, the technologies that we currently use in our products and services. Rapidly evolving technologies and new entrants in mobile and emerging payments pose a risk to Discover both as a card issuer and to the payments business. As a result, our future success may be dependent on our ability to identify and adapt to technological changes and evolving industry standards and to provide payment solutions for our customers, merchants and financial institution customers.

Difficulties or delays in the development, production, testing and marketing of new products or services may be caused by a number of factors including, among other things, operational, capital and regulatory constraints. The occurrence of such difficulties may affect the success of our products or services, and developing unsuccessful products and services could result in financial losses as well as decreased capital availability. In addition, the new products and services offered may not be attractive to consumers and merchant and financial institution customers. Also, success of a new product or service may depend upon our ability to deliver it on a large scale, which may require a significant capital investment that we may not be in a position to make. If we are unable to successfully introduce and maintain new income-generating products and services while also managing our expenses, it may impact our ability to compete effectively and materially adversely affect our business and earnings.

We rely on third parties to deliver services. If we face difficulties managing our relationships with third-party service providers, our revenue or results of operations could be materially adversely affected.

We depend on third-party service providers for many aspects of the operation of our business. For example, we depend on third parties for software and systems development, the timely transmission of information across our data transportation network, and for other telecommunications, processing, remittance, technology-related and other services in connection with our direct banking and payment services businesses. If a service provider fails to provide the services that we require or expect, or fails to meet contractual requirements, such as service levels or compliance with applicable laws, the failure could negatively impact our business by adversely affecting our ability to process customers' transactions in a timely and accurate manner, otherwise hampering our ability to serve our customers, or

subjecting us to litigation and regulatory risk for poor vendor oversight. Such a failure could adversely affect the perception of the reliability of our networks and services, and the quality of our brands, and could materially adversely affect our revenues and/or our results of operations.

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We rely on technology to deliver services. If key technology platforms become obsolete, or if we experience disruptions, including difficulties in our ability to process transactions, our revenue or results of operations could be materially adversely affected.

Our ability to deliver services to our customers and run our business in compliance with applicable laws and regulations may be affected by the functionality of our technology systems. The implementation of technology changes and upgrades to maintain current and integrated systems may result in compliance issues and may, at least temporarily, cause disruptions to our business, including, but not limited to, systems interruptions, transaction processing errors and system conversion delays, all of which could have a negative impact on us. In addition, our transaction processing systems and other operational systems may encounter service interruptions at any time due to system or software failure, natural disaster or other reasons. Such services could be disrupted at any of our primary or back-up facilities or our other owned or leased facilities. Third parties to whom we outsource the maintenance and development of certain technological functionality may experience errors or disruptions that could adversely impact us and over which we may have limited control. In addition, there is no assurance that we will be able to sustain our investment in new technology to avoid obsolescence of critical systems and applications. A failure to maintain current technology, systems and facilities or to control third-party risk, could cause disruptions in the operation of our business, which could materially adversely affect our transaction volumes, revenues, reputation and/or our results of operations.

Merchant defaults may adversely affect our business, financial condition, cash flows and results of operations.

As an issuer and merchant acquirer in the United States on the Discover Network, and as a holder of certain merchant agreements internationally for the Diners Club network, we may be contingently liable for certain disputed credit card sales transactions that arise between customers and merchants. If a dispute is resolved in the customer's favor, we will cause a credit or refund of the amount to be issued to the customer and charge back the transaction to the merchant or merchant acquirer. If we are unable to collect this amount from the merchant or merchant acquirer, we will bear the loss for the amount credited or refunded to the customer. Where the purchased product or service is not provided until some later date following the purchase, such as an airline ticket, the likelihood of potential liability increases. For the years ended December 31, 2014 and 2013 losses related to merchant chargebacks were not material.

Our success is dependent, in part, upon our executive officers and other key employees. If we are unable to recruit, retain and motivate key officers and employees to manage our business well, our business could be materially adversely affected.

Our success depends, in large part, on our ability to retain, recruit and motivate key officers and employees to manage our business. Our senior management team has significant industry experience and would be difficult to replace. We believe we are in a critical period of competition in the financial services and payments industry. The market for qualified individuals is highly competitive, and we may not be able to attract and retain qualified personnel or candidates to replace or succeed members of our senior management team or other key personnel. We may be subject to restrictions under future legislation or regulation limiting executive compensation. For example, the federal banking agencies issued guidance on incentive compensation policies at banking organizations. These requirements could negatively impact our ability to compete with other companies in recruiting and retaining key personnel and could impact our ability to offer incentives that motivate our key personnel to perform. If we are unable to recruit, retain and motivate key personnel to manage our business well, our business could be materially adversely affected.

Damage to our reputation could damage our business.

In recent years, financial services companies have experienced increased reputational risk as consumers protest and regulators scrutinize business and compliance practices of such companies. Maintaining a positive reputation is critical to attracting and retaining customers, investors and employees. Damage to our reputation can therefore cause significant harm to our business and prospects. Harm to our reputation can arise from numerous sources, including, among others, employee misconduct, litigation or regulatory outcomes, failing to deliver minimum standards of service and quality, compliance failures, and the activities of customers, business partners and counterparties. Social media also can cause harm to our reputation. By its very nature, social media can reach a wide audience in a very short amount of time, which presents unique corporate communications challenges. Negative or 'wrong' type of publicity generated through unexpected social media coverage can damage Discover's reputation and brand. Negative publicity

regarding us, whether or not true, may result in customer attrition and other harm to our business prospects.

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We may be unsuccessful in promoting and protecting our brands or protecting our other intellectual property, or third parties may allege that we are infringing their intellectual property rights.

The Discover, PULSE and Diners Club brands have substantial economic and goodwill value. Our success is dependent on our ability to promote and protect these brands and our other intellectual property. Our ability to attract and retain customers is highly dependent upon the external perception of our company and brands. Our brands are licensed for use to business partners and network participants, some of whom have contractual obligations to promote and develop our brands. For example, the Discover card brand is now being issued by certain Diners Club licensees in their local markets. If our business partners do not adhere to contractual standards, engage in improper business practices, or otherwise misappropriate, use or diminish the value of our brands or our other intellectual property, we may suffer reputational and financial damage. If we will not be able to adequately protect ourselves, our overall business success may be adversely affected. In addition, third parties may allege that our marketing, processes or systems may infringe their intellectual property rights. Given the potential risks and uncertainties of such claims, our business could be adversely affected by having to pay significant monetary damages or licensing fees, and we may have to alter our business practices.

Laws, regulations, and supervisory guidance and practices, or the application thereof, may adversely affect our business, financial condition and results of operations.

We must comply with an array of banking, consumer lending and payment services laws and regulations in all of the jurisdictions in which we operate as described more fully in “Business — Supervision and Regulation” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments.” Regulatory developments, findings and ratings could negatively impact our business strategies or require us to: limit or change our business practices, restructure our products in ways that we may not currently anticipate, limit our product offerings, invest more management time and resources in compliance efforts, limit the fees we can charge for services, or limit our ability to pursue certain business opportunities and obtain related required regulatory approvals. For additional information regarding bank regulatory limitations on acquisitions and investments, see "Business — Supervision and Regulation — Acquisitions and Investments." See Note 19: Litigation and Regulatory Matters to our consolidated financial statements for more information on recent matters affecting Discover and the second risk factor in this section regarding the regulatory environment for the businesses in which we engage. In addition, we are subject to inquiries and enforcement actions from state attorney general offices and regulation by the Federal Trade Commission, state banking regulators and the U.S. Department of Justice, as well as the SEC and New York Stock Exchange in our capacity as a public company. We also are subject to the requirements of entities that set and interpret the accounting standards (such as the FASB, the SEC, banking regulators and our independent registered public accounting firm) who may add new requirements or change their interpretations on how standards should be applied. A specific example of this is the proposed accounting standards update related to calculation of loan loss reserves. In December 2012, the FASB issued an exposure draft containing a current expected credit loss ("CECL") model for lenders and financial institutions to evaluate impairment of loans and financial instruments. The model as currently proposed requires evaluation of impairment based on an estimate of life of loan losses where the previous evaluation required utilization of an incurred loss model. The FASB is continuing to deliberate and refine the CECL model based on feedback received and a final standard is expected to be issued in 2015. While we continue to evaluate the model and provisions in the exposure draft and both are subject to change, this and other guidance not yet issued could potentially materially impact how we record and report our financial condition and results of operations, or could have an impact on regulatory capital. We are also subject to anti-corruption laws and regulations, including the U.S. Foreign Corrupt Practices Act and other laws, that prohibit the making or offering of improper payments. Failure to comply with laws, regulations and standards could lead to adverse consequences such as financial, structural, reputational and operational penalties, including receivership, litigation exposure and fines (as described further below). Failure to comply with anti-corruption and other laws can expose us and/or individual employees to potentially severe criminal and civil penalties. Legislative and regulatory changes could impact the profitability of our business activities, require us to limit or change our business practices or our product offerings, or expose us to additional costs (including increased compliance costs). Significant changes in laws and regulations may have a more adverse effect on our results of operations than on the results of our larger, more diversified competitors.

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Current and proposed laws and regulations addressing consumer privacy and data use and security could inhibit the number of payment cards issued and increase our costs.

Legal or regulatory pronouncements relating to consumer privacy, data use and security affect our business. We are subject to a number of laws concerning consumer privacy and data use and security. Due to recent consumer data compromise events in the United States, which resulted in unauthorized access to payment card data of millions of customers, these areas have become a focus of the executive administration, Congress, state legislators and banking regulators. Developments in this area, such as new laws or regulations, could result in requirements on Discover and other card issuers or networks that could increase costs or adversely affect the competitiveness of our credit card or debit card products. See the discussion on recent security developments in "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments — Payment Networks" for more information. In addition, failure to comply with the privacy and data use and security laws and regulations to which we are subject, including by reason of inadvertent disclosure of confidential information, could result in fines, sanctions, penalties or other adverse consequences and loss of consumer confidence, which could materially adversely affect our results of operations, overall business and reputation.

Litigation and regulatory actions could subject us to significant fines, penalties and/or requirements resulting in increased expenses.

Businesses in the consumer banking and payment services industries have historically been subject to significant legal actions, including class action lawsuits and commercial, shareholder and patent litigation. Many of these actions have included claims for substantial compensatory, statutory or punitive damages. While we have historically relied on our arbitration clause in agreements with customers to limit our exposure to consumer class action litigation, there can be no assurance that we will continue to be successful in enforcing our arbitration clause in the future. Legal challenges to the enforceability of these clauses have led most card issuers, and may cause us, to discontinue their use. There have been bills pending in Congress to directly or indirectly prohibit the use of pre-dispute arbitration clauses in some or all consumer banking products. Also, the Dodd-Frank Act authorized the CFPB to conduct a study on pre-dispute arbitration clauses and, based on the study, potentially limit or ban arbitration clauses. A preliminary report on arbitration agreements issued by the CFPB expressed concerns about these agreements that may signal the agency is contemplating taking such steps. Further, we are involved in pending legal actions challenging the use of our arbitration clause. In addition, we have been and may again be involved in various actions or proceedings brought by governmental regulatory and enforcement agencies, which could harm our reputation, require us to change our business activities and product offerings, or subject us to significant fines, penalties, customer restitution or other requirements, resulting in increased expenses. For example, complying with the FDIC consent order related to our anti-money laundering program causes us to incur significant expenses. See Note 19: Litigation and Regulatory Matters to our consolidated financial statements for more information on current matters affecting Discover.

Special Note Regarding Forward-Looking Statements

This annual report on Form 10-K and materials we have filed or will file with the SEC (as well as information included in our other written or oral statements) contain or will contain certain statements that are forward-looking within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Actual outcomes and results may differ materially from those expressed in, or implied by, our forward-looking statements. Words such as "expects," "anticipates," "believes," "estimates" and other similar expressions or future or conditional verbs such as "will," "should," "would" and "could" are intended to identify such forward-looking statements. You should not rely solely on the forward-looking statements and should consider all uncertainties and risks throughout this annual report on Form 10-K, including those described under "Risk Factors." The statements are only as of the date they are made, and we undertake no obligation to update any forward-looking statement.

Possible events or factors that could cause results or performance to differ materially from those expressed in our forward-looking statements include the following:

- changes in economic variables, such as the availability of consumer credit, the housing market, energy costs, the number and size of personal bankruptcy filings, the rate of unemployment, the levels of consumer confidence and consumer debt, and investor sentiment;

- the impact of current, pending and future legislation, regulation, supervisory guidance, and regulatory and legal actions, including, but not limited to, those related to financial regulatory reform, consumer financial services practices, anti-corruption and funding, capital and liquidity;

- the actions and initiatives of current and potential competitors;
- our ability to manage our expenses;
- our ability to successfully achieve card acceptance across our networks and maintain relationships with network participants;
- our ability to sustain and grow our private student loan and mortgage loan products;
- losses as a result of mortgage loan repurchase and indemnification obligations to secondary market purchasers;
- difficulty obtaining regulatory approval for, financing, closing, transitioning, integrating or managing the expenses of acquisitions of or investments in new businesses, products or technologies;
- our ability to manage our credit risk, market risk, liquidity risk, operational risk, compliance and legal risk, and strategic risk;
- the availability and cost of funding and capital;
- access to deposit, securitization, equity, debt and credit markets;
- the impact of rating agency actions;
- the level and volatility of equity prices, commodity prices and interest rates, currency values, investments, other market fluctuations and other market indices;
- losses in our investment portfolio;
- limits on our ability to pay dividends and repurchase our common stock;
- limits on our ability to receive payments from our subsidiaries;
- fraudulent activities or material security breaches of key systems;
- our ability to remain organizationally effective;
- our ability to increase or sustain Discover card usage or attract new customers;
- our ability to maintain relationships with merchants;
- the effect of political, economic and market conditions, geopolitical events and unforeseen or catastrophic events;
- our ability to introduce new products or services;
- our ability to manage our relationships with third-party vendors;
- our ability to maintain current technology and integrate new and acquired systems;
- our ability to collect amounts for disputed transactions from merchants and merchant acquirers;
- our ability to attract and retain employees;
- our ability to protect our reputation and our intellectual property; and
- new lawsuits, investigations or similar matters or unanticipated developments related to current matters.

We routinely evaluate and may pursue acquisitions of or investments in businesses, products, technologies, loan portfolios or deposits, which may involve payment in cash or our debt or equity securities.

The foregoing review of important factors should not be construed as exclusive and should be read in conjunction with the other cautionary statements that are included in this annual report on Form 10-K. These factors expressly qualify all subsequent oral and written forward-looking statements attributable to us or persons acting on our behalf. Except for any ongoing obligations to disclose material information as required under U.S. federal securities laws, we do not have any intention or obligation to update forward-looking statements after we distribute this annual report on Form 10-K, whether as a result of new information, future developments or otherwise.

Item 1B. Unresolved Staff Comments

None.

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Item 2. Properties

We have ten principal properties located in nine states in the United States. As of January 31, 2015, we owned four principal properties, which included our corporate headquarters, two call centers and a processing center, and we leased six principal properties, which included two call centers, our PULSE headquarters, two Discover Home Loans offices and a Student Loan Corporation office. The call centers, processing center and Student Loan Corporation offices largely support our Direct Banking segment; the PULSE headquarters is used by our Payment Services segment; the Discover Home Loans offices support our mortgage business; and our corporate headquarters is used by both our Direct Banking and Payment Services segments. Each of our call centers and our processing center are operating at and being utilized to a reasonable capacity. We believe our principal facilities are both suitable and adequate to meet our current and projected needs. We also have ten leased offices, seven of which are located outside the United States, that are used to support our Diners Club operations, and one leased office in China that supports our Direct Banking segment.

Item 3. Legal Proceedings

For a description of legal proceedings, see Note 19: Litigation and Regulatory Matters to our consolidated financial statements.

Item 4. Mine Safety Disclosures

None.

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Part II.

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Common Stock Market Prices and Dividends

Our common stock is traded on the New York Stock Exchange ("NYSE") (ticker symbol DFS). The approximate number of record holders of our common stock as of February 20, 2014 was 59,338.

The following table sets forth the quarterly high and low sales prices of a share of our common stock as reported by the NYSE and the cash dividends we declared per share of our common stock during the quarter indicated:

	Stock Price		Cash Dividends
	High	Low	Declared
Quarter Ended:			
March 31, 2013	$45.38	$37.24	$ —
June 30, 2013	$49.71	$42.12	$ 0.20
September 30, 2013	$53.36	$46.93	$ 0.20
December 31, 2013	$56.20	$48.40	$ 0.20
Quarter Ended:			
March 31, 2014	$60.00	$51.63	$ 0.20
June 30, 2014	$62.62	$54.35	$ 0.24
September 30, 2014	$65.98	$59.00	$ 0.24
December 31, 2014	$66.75	$60.15	$ 0.24

In the second quarter of 2014, we increased our quarterly common stock dividend from $0.20 per share to $0.24 per share and maintained a $0.24 per share dividend for each of the third and fourth quarters of 2014. Although we expect to continue our policy of paying regular cash dividends, we cannot assure that we will do so in the future. For more information, including conditions and limits on our ability to pay dividends, see "Business — Supervision and Regulation — Capital, Dividends and Share Repurchases," "Risk Factors — Credit, Market and Liquidity Risk — We may be limited in our ability to pay dividends on and repurchase our stock" and "— We are a holding company and depend on payments from our subsidiaries," "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Capital" and Note 17: Capital Adequacy to our consolidated financial statements.

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Issuer Purchases of Equity Securities

The table below sets forth information regarding purchases of our common stock related to our share repurchase program and employee transactions that were made by us or on our behalf during the most recent quarter:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan or Program[1]	Maximum Dollar Value of Shares that may yet be purchased under the Plans or Programs[1]
October 1-31, 2014				
Repurchase program[1]	2,406,623	$63.22	2,406,623	$2,321,590,369
Employee transactions[2]	1,338	$63.53	N/A	N/A
November 1-30, 2014				
Repurchase program[1]	1,795,445	$64.76	1,795,445	$2,205,316,932
Employee transactions[2]	217	$63.59	N/A	N/A
December 1-31, 2014				
Repurchase program[1]	2,036,490	$64.43	2,036,490	$2,074,099,410
Employee transactions[2]	2,534	$63.10	N/A	N/A
Total				
Repurchase program[1]	6,238,558	$64.06	6,238,558	$2,074,099,410
Employee transactions[2]	4,089	$63.27	N/A	N/A

(1) On April 16, 2014, our board of directors approved a share repurchase program authorizing the repurchase of up to $3.2 billion of our outstanding shares of common stock. This program expires on April 15, 2016 and may be terminated at any time.

(2) Reflects shares withheld (under the terms of grants under employee stock compensation plans) to offset tax withholding obligations that occur upon the delivery of outstanding shares underlying restricted stock units or upon the exercise of stock options.

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Stock Performance Graph

The following graph compares the cumulative total stockholder return (rounded to the nearest whole dollar) of our common stock, the S&P 500 Stock Index and the S&P 500 Financials Index for the period from November 30, 2009 through December 31, 2014. The graph assumes an initial investment of $100 on November 30, 2009. The cumulative returns include stock price appreciation and assume full reinvestment of dividends. This graph does not forecast future performance of our common stock.

	Discover Financial Services	S&P 500 Index	S&P 500 Financials Index
November 30, 2009	$100.00	$100.00	$100.00
November 30, 2010	$118.33	$107.75	$98.54
November 30, 2011	$154.34	$113.81	$87.53
November 30, 2012	$271.65	$129.26	$107.40
December 31, 2012(1)	$251.34	$130.17	$112.29
December 31, 2013	$367.71	$168.70	$149.58
December 31, 2014	$432.61	$187.92	$169.18

(1) In 2013, we changed fiscal years creating a one month transition period in December 2012.

Item 6. Selected Financial Data

The following table presents our selected financial data and operating statistics. The statement of income data for the calendar years ended December 31, 2014 and 2013, fiscal year ended November 30, 2012 and one month ended December 31, 2012 and the statement of financial condition data as of December 31, 2014 and 2013 have been derived from our audited consolidated financial statements included elsewhere in this annual report on Form 10-K. The statement of financial condition data as of November 30, 2012, 2011 and 2010, and the statement of income data for the fiscal years ended November 30, 2011 and 2010 have been derived from audited consolidated financial statements not included elsewhere in this annual report on Form 10-K.

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Discover Financial Services
Selected Financial Data

	For the Calendar Years Ended December 31,		For the Fiscal Years Ended November 30,			For the One Month Ended December 31, 2012
	2014	2013	2012	2011	2010	
	(dollars in millions, except per share amounts)					
Statement of Income Data:						
Interest income	$7,596	$7,064	$6,703	$6,345	$6,146	$595
Interest expense	1,134	1,146	1,331	1,485	1,583	103
Net interest income	6,462	5,918	5,372	4,860	4,563	492
Other income	2,015	2,306	2,281	2,205	2,095	200
Revenue net of interest expense	8,477	8,224	7,653	7,065	6,658	692
Provision for loan losses	1,443	1,086	848	1,013	3,207	178
Other expense	3,340	3,194	3,052	2,541	2,182	240
Income before income tax expense	3,694	3,944	3,753	3,511	1,269	274
Income tax expense	1,371	1,474	1,408	1,284	504	104
Net income	$2,323	$2,470	$2,345	$2,227	$765	$170
Net income allocated to common stockholders	$2,270	$2,414	$2,318	$2,202	$668	$168
Statement of Financial Condition Data (as of):						
Loan receivables[1]	$69,969	$65,771	$61,017	$57,670	$49,181	$62,598
Total assets	$83,126	$79,340	$75,283	$69,117	$61,130	$73,491
Total stockholders' equity	$11,134	$10,809	$9,778	$8,242	$6,457	$9,873
Allowance for loan losses	$1,746	$1,648	$1,725	$2,205	$3,304	$1,788
Long-term borrowings	$22,544	$20,474	$19,729	$18,287	$17,706	$17,666
Per Share of Common Stock:						
Basic EPS from continuing operations	$4.91	$4.97	$4.47	$4.06	$1.23	$0.34
Diluted EPS from continuing operations	$4.90	$4.96	$4.46	$4.06	$1.22	$0.34
Weighted-average shares outstanding (000's)	462,115	485,492	518,428	541,813	544,058	497,881
Weighted-average shares outstanding (fully diluted) (000's)	463,412	486,861	519,620	542,626	548,760	498,994
Dividends declared per share of common stock	$0.92	$0.60	$0.40	$0.20	$0.08	$0.14
Common stock dividend payout ratio	18.73 %	12.07 %	8.95 %	4.92 %	6.52 %	41.48 %
Ratios:						
Return on average total equity	21 %	24 %	26 %	30 %	12 %	21 %
Return on average assets	3 %	3 %	3 %	3 %	1 %	3 %
Average stockholders' equity to average total assets	14 %	14 %	13 %	12 %	11 %	14 %

(1) In 2011 we acquired $3.1 billion of student loan receivables acquired with the SLC acquisition in December 2010 and $2.4 billion of student loan receivables acquired from Citibank, N.A. in September 2011.

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Selected Financial Data (continued)

	For the Calendar Years Ended December 31,		For the Fiscal Years Ended November 30,			For the One Month Ended December 31, 2012
	2014	2013	2012	2011	2010	
	(dollars in millions)					
Selected Statistics:						
Total Loan Receivables						
Loan receivables	$69,969	$65,771	$61,017	$57,670	$49,181	$62,598
Average loan receivables	$65,853	$61,820	$58,043	$53,260	$50,203	$61,877
Interest yield	11.40 %	11.28 %	11.38 %	11.78 %	12.13 %	11.21 %
Net principal charge-off rate	2.04 %	1.98 %	2.29 %	3.97 %	7.53 %	2.19 %
Delinquency rate (over 30 days)	1.66 %	1.64 %	1.75 %	2.29 %	3.87 %	1.69 %
Delinquency rate (over 90 days)	0.78 %	0.77 %	0.83 %	1.14 %	2.02 %	0.82 %
Credit Card Loans						
Credit card loan receivables	$56,128	$53,150	$49,642	$46,972	$45,502	$51,135
Average credit card loan receivables	$52,600	$49,816	$47,301	$45,522	$45,911	$50,494
Interest yield	12.09 %	12.00 %	12.16 %	12.42 %	12.71 %	11.92 %
Net principal charge-off rate	2.27 %	2.21 %	2.62 %	4.47 %	8.02 %	2.47 %
Delinquency rate (over 30 days)	1.73 %	1.72 %	1.86 %	2.38 %	4.02 %	1.79 %
Delinquency rate (over 90 days)	0.85 %	0.84 %	0.91 %	1.19 %	2.11 %	0.90 %
Personal Loans						
Personal loan receivables	$5,007	$4,191	$3,272	$2,648	$1,878	$3,296
Average personal loan receivables	$4,592	$3,706	$2,944	$2,228	$1,593	$3,290
Interest yield	12.36 %	12.52 %	12.35 %	11.94 %	11.41 %	12.43 %
Net principal charge-off rate	2.04 %	2.13 %	2.33 %	3.02 %	5.72 %	2.52 %
Delinquency rate (over 30 days)	0.79 %	0.70 %	0.76 %	0.87 %	1.57 %	0.77 %
Delinquency rate (over 90 days)	0.22 %	0.21 %	0.23 %	0.28 %	0.57 %	0.23 %
Private Student Loans (excluding PCI)						
Private student loan receivables	$4,850	$3,969	$3,000	$2,069	$999	$3,072
Average private student loan receivables	$4,450	$3,561	$2,557	$1,637	$827	$3,021
Interest yield	7.02 %	7.07 %	7.20 %	7.04 %	5.75 %	7.22 %
Net principal charge-off rate	1.29 %	1.30 %	0.73 %	0.48 %	0.33 %	0.81 %
Delinquency rate (over 30 days)	1.80 %	1.66 %	1.07 %	0.63 %	0.50 %	1.22 %
Delinquency rate (over 90 days)	0.52 %	0.46 %	0.27 %	0.14 %	0.14 %	0.29 %

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our audited consolidated financial statements and related notes included elsewhere in this annual report on Form 10-K. Some of the information contained in this discussion and analysis constitutes forward-looking statements that involve risks and uncertainties. Actual results could differ materially from those discussed in these forward-looking statements. Factors that could cause or contribute to these differences include, but are not limited to, those discussed below and elsewhere in this annual report on Form 10-K particularly under "Risk Factors" and "Special Note Regarding Forward-Looking Statements," which immediately follows "Risk Factors." Unless otherwise specified, references to Notes to our consolidated financial statements are to the Notes to our audited consolidated financial statements as of December 31, 2014 and 2013 and for calendar years ended December 31, 2014 and 2013, fiscal year ended November 30, 2012 and one month ended December 31, 2012.

Introduction and Overview

Discover Financial Services is a direct banking and payment services company. We provide direct banking products and services and payment services through our subsidiaries. We offer our customers credit card loans, private student loans, personal loans, home loans, home equity loans and deposit products. We also operate the Discover Network, the PULSE network ("PULSE") and Diners Club International ("Diners Club"). The Discover Network processes transactions for Discover-branded credit cards and provides payment transaction processing and settlement services. PULSE operates an electronic funds transfer network, providing financial institutions issuing debit cards on the PULSE network with access to ATMs domestically and internationally, as well as point-of-sale terminals at retail locations throughout the U.S. for debit card transactions. Diners Club is a global payments network of licensees, which are generally financial institutions, that issue Diners Club branded charge cards and/or provide card acceptance services.

Our primary revenues consist of interest income earned on loan receivables and fees earned from customers, merchants and issuers. The primary expenses required to operate our business include funding costs (interest expense), loan loss provisions, customer rewards, and expenses incurred to grow, manage and service our loan receivables and networks. Our business activities are funded primarily through consumer deposits, securitization of loan receivables and the issuance of unsecured debt.

Change in Fiscal Year

On December 3, 2012, our board of directors approved a change in our fiscal year end from November 30 to December 31 of each year. This fiscal year change was effective January 1, 2013. As a result of the change, we had a one month transition period in December 2012. The audited results for the one month ended December 31, 2012 is included in this report.

2014 Highlights

- Net income was $2.3 billion, compared to $2.5 billion in the prior year.
- Total loans grew $4.2 billion, or 6.4%, from the prior year to $70.0 billion.
- Credit card loans grew $3.0 billion, or 5.6%, to $56.1 billion and Discover card sales volume increased 5.1% from the prior year.
- Net charge-off rate for credit card loans increased 6 basis points from the prior year to 2.27% and the delinquency rate for credit card loans over 30 days past due increased 1 basis point to 1.73%.
- Payment Services transaction dollar volume for the segment was $202.3 billion, up 3% from the prior year.
- We incurred a $178 million charge to earnings to enhance our rewards program by allowing easier redemption of rewards, which resulted in the elimination of our current estimate of customer rewards forfeiture.
- Our capital market activities included issuances of approximately $5.0 billion in public credit card asset-backed securities. Discover Bank issued $1.1 billion in senior bank notes and Discover Financial Services issued $500 million of senior notes.
- We repurchased approximately 25 million shares, or 5%, of our outstanding common stock for $1.5 billion.

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2013 and 2012 Highlights

- During the 2013 calendar year, our capital market activities included issuances of approximately $4.7 billion in public credit card asset-backed securities. Discover Bank issued $1.7 billion in senior bank notes.
- We repurchased approximately 27 million shares of common stock for $1.3 billion, reducing our number of shares outstanding by 5% during the calendar year ended December 31, 2013.
- We began offering residential mortgage loans through Discover Home Loans following our June 2012 acquisition of substantially all of the operating and related assets of Home Loan Center, a subsidiary of Tree.com, Inc.
- We repurchased 34 million shares, or approximately 6%, of our outstanding common stock for $1.2 billion during the fiscal year ended November 30, 2012.
- During the 2012 fiscal year, our capital market activities included issuances of approximately $5.4 billion in public credit card asset-backed securitizations and a $560 million preferred stock issuance. We also completed two private debt exchange offers involving an aggregate $822 million of outstanding debt.

Outlook

The growth of our existing direct banking products remains a priority as we continue to enhance our offerings to customers. We anticipate that investments in marketing and the fourth quarter 2014 changes we made to simplify and ease reward redemption will contribute to new card account growth and wallet share gains with existing customers. We are also targeting solid growth in our private student and personal loan portfolios, and are evaluating our home loans strategy.

Revenue margin is expected to decline modestly in 2015. We expect this to be driven by net interest margin compression, a continued decline in protection products revenue, an increased credit card rewards rate and challenges in our payments business. The anticipated net interest margin compression is due to expected higher funding costs and modest yield declines from growth in promotional balances, run-off of higher priced balances and higher interest charge-offs.

While our credit quality remains relatively stable, we increased our allowance for loan losses in the fourth quarter of 2014 due to seasoning of loan growth from recent years. We expect our provision levels to increase as a result of continued seasoning of and growth in our loan portfolio.

We expect operating expenses to increase in 2015, primarily due to planned marketing, technology and infrastructure investments, as well as increased legal, regulatory and compliance costs. Specifically, our anti-money laundering program enhancements are expected to contribute to increased expenses.

We expect lower returns in our payment services segment in 2015 due to competitive challenges, the loss of network relationships and increased expenses. We continue to face substantial and intense competition in the payments industry, which impacts our revenue margins, transaction volume and business strategies. We anticipate a decline in volume in 2015 as compared to prior year periods as a result of a previously disclosed third-party issuer contract related to our Network Partners business that was not renewed in 2014 and the loss of volume from a large PULSE debit issuer. The loss of volumes and increase in expenses is expected to significantly impact the financial results of our payment services segment, but is not expected to significantly impact our overall profitability. Despite these continued challenges in our payments business, we continue to leverage our network to support our card-issuing business.

Regulatory Environment and Developments

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") contains comprehensive provisions governing the practices and oversight of financial institutions and other participants in the financial markets. The Dodd-Frank Act regulates large systemically significant financial firms, including Discover, through a variety of measures, including increased capital and liquidity requirements, limits on leverage and enhanced supervisory authority. Federal banking regulators have implemented and continue to propose new regulations and supervisory guidance under the Dodd-Frank Act and otherwise, and have been increasing their examination and enforcement action activities. We expect regulators to continue taking formal enforcement actions against financial institutions in addition to addressing concerns through non-public supervisory actions or findings.

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The impact of the evolving regulatory environment on our business and operations depends upon a number of factors including supervisory priorities and actions, the actions of our competitors and other marketplace participants and the behavior of consumers. Regulatory developments, findings and ratings could negatively impact our business strategies, require us to limit or change our business practices, limit our product offerings, invest more management time and resources in compliance efforts, limit the fees we can charge for services, or limit our ability to pursue certain business opportunities and obtain related required regulatory approvals. For additional information regarding bank regulatory limitations on acquisitions and investments, see "Business — Supervision and Regulation — Acquisitions and Investments." For more information on recent matters affecting Discover, see Note 19: Litigation and Regulatory Matters to our consolidated financial statements. Regulatory developments could also impact our strategies, the value of our assets, or otherwise adversely affect our businesses.

Compliance expenditures have increased significantly for Discover and other financial services firms, and we expect them to continue to increase as regulators remain focused on controls and operational processes. We may face additional compliance and regulatory risk to the extent that we enter into new business arrangements with third-party service providers, alternative payment providers or other industry participants. The additional expense, time and resources needed to comply with ongoing regulatory requirements may adversely impact our business and results of operations.

The final rule implementing Section 619 of the Dodd-Frank Act, commonly referred to as the Volcker Rule, which contains certain prohibitions and restrictions on the ability of “banking entities” to engage in proprietary trading and sponsor or invest in “covered funds” became effective in April 2014, and banking entities must generally conform with this rule by July 2015, subject to a one-year extension for certain investments in, and relationships with, legacy covered funds. We do not engage in any of the activities that are prohibited by the final rule and, therefore, do not believe it will have a material impact on our business.

Consumer Financial Services

The CFPB regulates consumer financial products and services, as well as certain financial services providers, including Discover. The CFPB is authorized to prevent “unfair, deceptive or abusive acts or practices” and ensure consistent enforcement of laws so that all consumers have access to markets for consumer financial products and services that are fair, transparent and competitive. The CFPB has rulemaking and interpretive authority under the Dodd-Frank Act and other federal consumer financial services laws, as well as broad supervisory, examination and enforcement authority over large providers of consumer financial products and services, such as Discover. The CFPB collects detailed account level information from us about credit cards, deposit accounts and other products, and is authorized to collect fines and provide consumer restitution in the event of violations. Several of our products, including credit cards, private student loans and home loans, are areas of focus by the CFPB. In addition, the CFPB has an online complaint system that allows consumers to log public complaints with respect to the products we offer. The CFPB has proposed making consumer narratives available to the public. The financial services industry is concerned that the publication of detailed unverified consumer narratives could lead to reputational injury to consumer lenders. The CFPB's analysis of account data and complaints could inform future decisions with respect to regulatory, enforcement or examination focus, and influence consumers' attitudes about doing business with Discover.

Credit Cards

The CFPB has been focused recently on online credit card disclosures, the clarity and transparency of credit card rewards and grace period disclosures, and debt collection practices. In September 2014, the CFPB issued guidance on the marketing of credit card promotional interest rate offers that will require enhanced consumer disclosures. The CFPB is currently collecting data about reward program marketing practices, which may result in additional guidance. Further, the CFPB continues to collect data regarding consumers' experiences with debt collectors and plans to use the data to help develop debt collection regulations. Courts and legislators have also been focused on the debt collection practices of consumer financial services providers. The ultimate impact of the increased scrutiny of these areas is uncertain at this time.

Private Student Loans

There continues to be significant legislative and regulatory focus on the private student loan market, including by the CFPB and the FDIC. This regulatory focus has resulted in an increase in supervisory examinations of Discover related

to private student loans. The CFPB is currently investigating certain student loan servicing practices of Discover Bank. See Note 19: Litigation and Regulatory Matters to our consolidated financial statements for more information. The

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recent legislative and regulatory areas of focus include servicing practices with respect to assisting student borrowers with economic hardships, refinancing of private student loans, the liability of student borrowers in the event of cosigner death or bankruptcy, the standard for discharging student loans in bankruptcy, loan payment allocation, and requirements related to borrower military service. In October 2014, the CFPB student loan ombudsman for the private student loan market issued the 2014 annual report required by the Dodd-Frank Act, which referenced these issues and others. The enactment of new legislation or the adoption of new regulations or guidance may increase the complexity and expense of servicing student loans. Legislators and regulators may take additional actions that impact the student loan market in the future, which could cause us to restructure our private student loan product in ways that we may not currently anticipate.

Mortgage Lending

The CFPB has indicated that the mortgage industry is an area of supervisory focus and that it will concentrate its examinations and rulemaking efforts on the variety of mortgage-related topics required under the Dodd-Frank Act including steering consumers to less favorable products, discrimination, abusive or unfair lending practices, predatory lending, origination disclosures, minimum mortgage underwriting standards, mortgage loan origination compensation and servicing practices. The CFPB has published several final rules impacting the mortgage industry, including rules related to ability-to-repay, mortgage servicing and integrated mortgage origination disclosures. Failure to comply with the ability-to-repay rule could result in possible CFPB enforcement action and special statutory damages plus actual, class action and attorney fee damages, all of which a borrower may claim in defense of a foreclosure action at any time. The new integrated mortgage origination disclosures rule, effective August 2015, requires combining disclosures currently provided under the Truth in Lending Act and the Real Estate Settlement Procedures Act, resulting in significant effort by the mortgage industry to test and implement as well as process changes with third-party settlement agents. In addition, congressional committees have approved legislation that could significantly affect the single family housing finance market in the United States, including proposals to wind down the government-sponsored enterprises, Fannie Mae and Freddie Mac, to which we currently sell our mortgages. It is uncertain what the ultimate impact of these developments will be on our mortgage business.

In October 2014, the Federal Reserve, FDIC, SEC and other federal regulatory agencies adopted a final rule to implement requirements under the Securities Exchange Act of 1934, as added under the Dodd-Frank Act, exempting "qualified residential mortgages" from the requirement that the sponsor of an asset-backed securitization retain not less than five percent of the credit risk of the underlying assets. Because most of the mortgages we offer are "qualified residential mortgages" as defined in the exemption, we do not expect the final rule to impact the pricing and depth of the secondary mortgage market to which we sell our mortgages.

Payment Networks

The Dodd-Frank Act contains several provisions impacting the debit card market, including network participation requirements and interchange fee limitations. The changing debit card environment, including competitor actions related to merchant and acquirer pricing and transaction routing strategies, has adversely affected and is expected to continue to adversely affect our PULSE network's business practices, network transaction volume, revenue and prospects for future growth. We continue to closely monitor competitor strategies in order to assess their impact on our business and on competition in the marketplace. The U.S. Department of Justice is examining some of these competitor pricing strategies. In addition, the Dodd-Frank Act's network participation requirements impact PULSE's ability to enter into exclusivity arrangements, which affect PULSE's current business practices and may materially adversely affect its network transaction volume and revenue.

Publicly-reported incidents regarding unauthorized access to consumer information held by major retailers and others has prompted a renewed focus by Congress and state legislators to possibly enact legislation to address future data security breaches. In October 2014, the President signed a new Executive Order which, among other things, directs the government to take the lead in moving the market towards more secure payment systems, including implementing a new policy to secure payments to and from the federal government by applying chip and PIN technology to newly issued and existing government credit cards and debit cards, and upgrading retail payment card terminals at federal agency facilities to accept chip and PIN-enabled cards. In January 2015, the President announced legislative proposals and administration efforts with respect to privacy and cybersecurity, including a specific proposal for a national data

breach notification standard and a proposal designed to encourage the private sector to increase the sharing of information related to cyber threats. All these developments could ultimately result in the imposition of requirements on Discover or other card issuers or networks that could increase costs or adversely affect the

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competitiveness of our credit card or debit card products. It is too early to know if any new legislation will become law, the final form any such legislation would take, or the impact such a law would have on Discover.

The final compromise text for the proposed European Union regulation of interchange fees assessed for card-based payment transactions was released and endorsed by the European Union countries in January 2015. The regulation remains subject to a vote by the full European Parliament and final approval by the Council anticipated in April 2015. The regulation, if enacted, would reduce the fees that card issuers can receive for payment card transactions. As such, the regulation would likely have significant impact across the industry and could impact our Diners Club network. At this time, we are evaluating the scope and impact that the regulation would have on the business practices and revenues of our Diners Club network participants in Europe.

Capital, Liquidity and Funding

Capital

Discover Financial Services and Discover Bank are subject to new regulatory capital requirements beginning in January 2015 under final rules issued by the Federal Reserve and the FDIC to implement the provisions of the Basel III regulatory capital reforms. The rules include significant changes to bank capital, leverage and liquidity requirements. The rules require new risk-based capital and leverage ratios and refine the definition of what constitutes capital for purposes of calculating those ratios. See "Business — Supervision and Regulation — Capital, Dividends and Share Repurchases" for more information. In addition, the rules establish a capital conservation buffer above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital and result in higher required minimum ratios by up to 2.5%. The new capital conservation buffer requirement will be phased in beginning in January 2016 and will be fully implemented in January 2019. A banking organization will be subject to limitations on paying dividends, engaging in share repurchases and paying discretionary bonuses if its capital level falls below any of the minimum capital requirements, including the buffer amount. Based on our current capital composition and levels, we believe that we would be in compliance with the requirements as set forth in the final rules had they been in effect prior to 2015.

The final rule implementing the Federal Reserve's amendments to the capital plan and stress test rules applicable to bank holding companies with $50 billion or more in total consolidated assets, including Discover, became effective in November 2014. The rule provides guidance with respect to the current capital plan and stress testing cycle. It also modifies the start date of the capital plan and stress test cycles from October 1 of a calendar year to January 1 of the following calendar year, with capital plans and stress testing results due April 5 instead of January 5, starting in 2016. The final rule also clarifies the limitations that apply on capital distributions where a bank holding company has net capital issuances that are less than the amount in that bank holding company's approved capital plan.

Liquidity

We are subject to the Federal Reserve's final rule implementing certain enhanced prudential standards under the Dodd-Frank Act for large U.S. bank holding companies, including enhanced liquidity and risk management requirements, which became effective beginning in January 2015. The final rule prescribes a broad range of qualitative liquidity risk management practices.

Additionally, in September 2014, federal banking regulators published a final rule to implement the liquidity coverage ratio as a new quantitative requirement designed to promote the short-term resilience of the liquidity risk profile of large and internationally active banking organizations in the United States. The ratio requires covered banks to maintain an amount of high-quality liquid assets sufficient to cover projected net cash outflows during a prospective 30-day calendar period under an acute, hypothetical liquidity stress scenario. We are subject to this new requirement and will be required to maintain a liquidity ratio of 90% in 2016, which will increase to 100% in 2017. We believe our liquidity management practices position us well to comply with this new standard when it becomes effective.

In October 2014, the Basel Committee on Banking Supervision issued the final standard for the Net Stable Funding Ratio (“NSFR”). The NSFR is defined as the amount of available stable funding relative to the amount of required stable funding. “Available stable funding” is defined as the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR, which extends to one year. This ratio should be equal to at least 100% on an ongoing basis. The NSFR limits overreliance on short-term wholesale funding, encourages better assessment of funding risk across all on- and off-balance sheet items, and promotes funding stability. The rule is expected to be fully

implemented beginning in January 2018. At this time, the U.S. regulatory authorities are still

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assessing the NSFR. These new standards are subject to the Federal Reserve's adaptation for U.S. banks, and their terms may change before implementation.

Securitizations

In August 2014, the SEC adopted final rules for asset-backed securities offerings that will substantially change the disclosure, reporting and offering process for public offerings of asset-backed securities, including those offered under Discover Bank's credit card securitization program. The new rules will change the disclosure and offering process for credit card securitizations and the eligibility criteria for shelf registration statements. Among other changes, the final rules will require a certification concerning the disclosure contained in the prospectus and the design of the securitization at the time of each offering off the shelf and appointment of an asset representations reviewer to review assets for compliance with related representations and warranties in the related underlying transaction agreements when delinquency rates rise above a certain level and investors request such a review. Issuers of publicly offered asset-backed securities must comply with these new rules no later than November 23, 2015. We do not believe these rules will have a material impact on Discover Bank's securitization program.

In October 2014, the Federal Reserve, FDIC, SEC and other federal regulatory agencies adopted a final rule to implement requirements under the Securities Exchange Act of 1934, as added by the Dodd-Frank Act, requiring the sponsor of an asset-backed securitization to retain not less than five percent of the credit risk of the underlying assets. Sponsors of asset-backed securitizations will be required to comply with the risk retention rules no later than December 24, 2016. We do not believe the risk retention rules will have a material impact on Discover Bank's securitization program.

Results of Operations

The discussion below provides a summary of our results of operations for the calendar year ended December 31, 2014 compared to our results of operations for the calendar year ended December 31, 2013 and fiscal year ended November 30, 2012. The discussion also provides information about our loan receivables as of December 31, 2014 compared to December 31, 2013 and December 31, 2012.

Segments

We manage our business activities in two segments: Direct Banking and Payment Services. In compiling the segment results that follow, our Direct Banking segment bears all corporate overhead costs that are not specifically associated with a particular segment and all costs associated with Discover Network marketing, servicing and infrastructure, with the exception of an allocation of direct and incremental costs driven by our Payment Services segment.

Direct Banking

Our Direct Banking segment includes Discover-branded credit cards issued to individuals on the Discover Network and other consumer products and services, including private student loans, personal loans, home loans, home equity loans, prepaid cards and other consumer lending and deposit products. The majority of Direct Banking revenues relate to interest income earned on the segment's loan products. Additionally, our credit card products generate substantially all of our revenues related to discount and interchange, protection products and loan fee income.

Payment Services

Our Payment Services segment includes PULSE, an automated teller machine, debit and electronic funds transfer network; Diners Club, a global payments network; and our Network Partners business, which provides payment transaction processing and settlement services on the Discover Network. This segment also includes the business operations of Diners Club Italy, which primarily consist of issuing Diners Club charge cards. The majority of Payment Services revenues relate to transaction processing revenue from PULSE and royalty and licensee revenue (included in other income) from Diners Club.

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The following table presents segment data (dollars in millions):

	For the Calendar Years Ended December 31,		For the Fiscal Year Ended November 30, 2012	For the One Month Ended December 31, 2012
	2014	2013		
Direct Banking				
Interest income				
Credit card	$6,359	$5,978	$5,751	$510
Private student loans	312	252	184	18
PCI student loans	260	272	303	24
Personal loans	568	464	363	34
Other	97	98	102	9
Total interest income	7,596	7,064	6,703	595
Interest expense	1,134	1,146	1,331	103
Net interest income	6,462	5,918	5,372	492
Provision for loan losses	1,440	1,069	848	178
Other income	1,700	1,976	1,939	169
Other expense	3,117	2,961	2,891	224
Income before income tax expense	3,605	3,864	3,572	259
Payment Services				
Provision for loan losses	3	17	—	—
Other income	315	330	342	31
Other expense	223	233	161	16
Income before income tax expense	89	80	181	15
Total income before income tax expense	$3,694	$3,944	$3,753	$274

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The following table presents information on transaction volume (in millions):

	For the Calendar Years Ended December 31,		For the Fiscal Year Ended November 30, 2012	For the One Month Ended December 31, 2012
	2014	2013		
Network Transaction Volume				
PULSE Network	$165,851	$159,805	$159,944	$14,133
Network Partners	9,446	9,808	8,754	885
Diners Club[1]	26,970	26,867	28,644	2,274
Total Payment Services	202,267	196,480	197,342	17,292
Discover Network—Proprietary[2]	119,471	113,791	109,014	10,987
Total Volume	$321,738	$310,271	$306,356	$28,279
Transactions Processed on Networks				
Discover Network	2,020	1,947	1,844	183
PULSE Network	4,283	4,187	4,321	357
Total	6,303	6,134	6,165	540
Credit Card Volume				
Discover Card Volume[3]	$125,111	$118,594	$114,213	$11,384
Discover Card Sales Volume[4]	$115,518	$109,957	$105,454	$10,657

(1) Diners Club volume is derived from data provided by licensees for Diners Club branded cards issued outside North America and is subject to subsequent revision or amendment.
(2) Represents gross proprietary sales volume on the Discover Network.
(3) Represents Discover card activity related to net sales, balance transfers, cash advances and other activity.
(4) Represents Discover card activity related to net sales.

Direct Banking

For the Year Ended December 31, 2014 compared to the Year Ended December 31, 2013

Our Direct Banking segment reported pretax income of $3.6 billion for the year ended December 31, 2014, as compared to pretax income of $3.9 billion for the year ended December 31, 2013.

Loan receivables totaled $69.9 billion at December 31, 2014, which was up from $65.8 billion at December 31, 2013, due to growth in credit card loans and other loan portfolios partially offset by a decrease in purchased credit-impaired ("PCI") student loan balances. The growth in credit card loans was due to growth in customers with revolving balances partially offset by a higher net principal charge-off rate. The growth within the other loans portfolio was primarily attributable to organic growth in personal and private student loans. Discover card sales volume was $115.5 billion for the year ended December 31, 2014, which was an increase of 5% as compared to the year ended December 31, 2013. This volume growth was driven primarily by continued growth in new accounts combined with lower attrition.

Net interest margin increased for the year ended December 31, 2014 as compared to the year ended December 31, 2013. This was primarily driven by higher yields on total loan receivables combined with lower interest rates on funding. The increase in loan receivable yields was driven by higher interest rates and growth in non-promotional revolving balances, partially offset by decline in higher rate balances along with growth in credit card promotional balances.

Interest income increased during the year ended December 31, 2014 as compared to the year ended December 31, 2013 primarily due to higher average balances of credit card loans, personal loans and private student loans resulting from growth across these products. The increase was also attributable to higher yields on credit card loans and PCI student loans, partially offset by a decrease in yield on personal loans along with a decrease in PCI student loan balances.

Interest expense was relatively flat during the year ended December 31, 2014 as compared to the year ended December 31, 2013, as lower interest expense on deposits attributable to lower yields was offset by higher interest

expense resulting from increase in borrowings.

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At December 31, 2014 and December 31, 2013, our delinquency rate for credit card loans over 30 days past due was 1.73% and 1.72%, respectively. For the year ended December 31, 2014, our net charge-off rate on credit cards remained relatively flat as compared to the year ended December 31, 2013. Recent loan growth has led to an increase in reserves required to cover losses from loan seasoning. An increase in reserve requirements combined with lower recoveries led to an increase in the provision for loan losses for the year ended December 31, 2014, as compared to the year ended December 31, 2013. For a more detailed discussion on provision for loan losses, see "— Loan Quality — Provision and Allowance for Loan Losses."

Total other income decreased for the year ended December 31, 2014 as compared to the year ended December 31, 2013 primarily due to a one-time charge to customer rewards costs resulting from the elimination of our current estimate of customer rewards forfeiture of $178 million, which reduced discount and interchange revenue. Gain on sale of mortgage loans also decreased, driven primarily by lower mortgage refinance volume due to increased mortgage interest rates in 2013, as well as changes in product mix. The overall decrease in other income was also attributable to a decrease in protection product revenue reflecting lower sales volume as we have stopped selling these products.

Total other expense increased for the year ended December 31, 2014 as compared to the year ended December 31, 2013. The increase was primarily due to higher employee compensation costs driven by growth in headcount, along with higher professional fees related to technology and digital investments. Marketing and business development costs, and information processing and communications costs also increased due to growth initiatives. The goodwill impairment of $27 million related to the Discover Home Loans business also contributed to overall increase in total other expenses. For more information, see Note 7: Goodwill and Intangible Assets to our consolidated financial statements.

For the Calendar Year Ended December 31, 2013 compared to the Fiscal Year Ended November 30, 2012

Our Direct Banking segment reported pretax income of $3.9 billion for the calendar year ended December 31, 2013, as compared to pretax income of $3.6 billion for the fiscal year ended November 30, 2012.

Loan receivables totaled $65.8 billion at December 31, 2013, which was up from $62.6 billion at December 31, 2012, due to growth in credit card loans and other loan portfolios partially offset by a decrease in PCI loans balances. The growth in credit card loans was due to growth in customers with revolving balances combined with a continued improvement in the net principal charge-off rate. The growth within the other loans portfolio was primarily attributable to organic growth in personal and private student loans. Discover card sales volume was $110.0 billion for the calendar year ended December 31, 2013, which was an increase of 4% as compared to the fiscal year ended November 30, 2012. This increase was driven primarily by continued growth in our active customer base combined with seasonal promotional programs driving incremental sales.

Net interest margin increased for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012. This was primarily driven by decreased funding costs and growth in loan receivables, partially offset by lower yields on total loan receivables. The decrease in loan receivable yields was driven by growth in credit card promotional balances and a decline in higher rate balances, partially offset by growth in non-promotional revolving balances.

Interest income increased during the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily due to higher average balances of credit card loans, personal loans and private student loans resulting from growth across these products combined with lower credit card loan interest charge-offs. The increase in interest income from these products was partially offset by a decrease in yield on credit card loan receivables along with a decrease in PCI student loan volume.

Interest expense declined during the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily due to lower funding costs resulting from maturities of higher interest borrowings and deposits that were replaced with borrowings and deposits paying low interest rates.

At December 31, 2013, our delinquency rate for credit card loans over 30 days past due was 1.72% as compared to 1.79% at December 31, 2012, reflective of continuing trends of strong credit performance. For the calendar year ended December 31, 2013, our net charge-off rate on credit cards declined to 2.21%, as compared to 2.62% for the fiscal year ended November 30, 2012. An increase in reserve requirements partially offset by a decline in the level of net

charge-offs led to an increase in the provision for loan losses for the calendar year ended December 31, 2013, as compared to the fiscal year ended November 30, 2012. For a more detailed discussion on provision for loan losses, see "— Loan Quality — Provision and Allowance for Loan Losses."

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Total other income increased for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily due to an increase in discount and interchange revenue, which was driven by an increase in sales volume. Gain on sale of mortgage loans also increased, reflecting a full year of activity for the calendar year ended December 31, 2013 as compared to a partial year of activity for the fiscal year ended November 30, 2012, due to the acquisition and integration of assets of Home Loan Center in June of 2012. The overall increase in other income was partially offset by a decrease in protection product revenue reflecting lower sales volume as we have stopped selling these products. Loan fee income also decreased due to lower levels of delinquencies which resulted in a lower level of loan fees being generated. Additionally, the increase was partially offset by decrease in refinance mortgage loan volume due to increasing interest rates during 2013.

Total other expense increased for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily due to an increase in employee compensation costs driven by increased headcount. Marketing and business development costs also increased due to growth initiatives. Higher information processing and communication expenses also contributed to the increase as a result of higher software maintenance, licenses, and technology expenses due to growth initiatives. The overall expense increase was partially offset by legal expenses associated with the consent order that Discover Bank entered into with the FDIC and CFPB, for which there was no equivalent impact in 2013.

Payment Services

For the Year Ended December 31, 2014 compared to the Year Ended December 31, 2013

Our Payment Services segment reported pretax income of $89 million for the year ended December 31, 2014, up $9 million as compared to the year ended December 31, 2013, primarily as the result of a decrease in loan losses related to certain Diners Club licensee loans and other expense, partially offset by a decrease in other income. The decrease in other expense was primarily due to non-recurring expenses incurred in 2013 related to our purchase of the Diners Club Italy licensee and financial assistance to facilitate the purchase of the Slovenian licensee by a European bank. The decrease in other expense was partially offset by a fair value adjustment of $21 million resulting from recording Diners Club Italy as held-for-sale in 2014. The decrease in other income was primarily driven by a decrease in transaction processing revenue reflecting the impact of merchant rerouting and lower rates.

Transaction dollar volume increased $5.8 billion for the year ended December 31, 2014 as compared to the year ended December 31, 2013, primarily driven by a growth in PULSE network volume. The number of transactions processed on the PULSE network increased slightly for the year ended December 31, 2014 as compared to the year ended December 31, 2013.

We have been working with our European Diners Club licensees with regard to their ability to maintain financing sufficient to support business operations. We may provide additional support in the future, including loans, facilitating transfer of ownership, or acquiring assets or licenses, which may cause us to incur losses. The licensees that we currently consider to be of concern accounted for approximately 4% of Diners Club revenue for the year ended December 31, 2014. In addition, Diners Club has $151 million of non-amortizable intangible assets at December 31, 2014. While we determined that none of these intangibles are presently impaired, to the extent that we are unable to maintain Diners Club revenues at appropriate levels, we may be exposed to a non-cash impairment loss on these assets that, when recognized, could have a material adverse impact on our results of operations.

For the Calendar Year Ended December 31, 2013 compared to the Fiscal Year Ended November 30, 2012

Our Payment Services segment reported pretax income of $80 million for the calendar year ended December 31, 2013, down $101 million as compared to the fiscal year ended November 30, 2012, primarily as the result of an increase in other expense and to a lesser extent a decrease in other income. The increase in other expense was primarily due to an increase in expenses attributable to support of our Diners Club network and in employee compensation reflecting an increase in headcount. The decrease in other income was primarily driven by a decrease in transaction processing revenue reflecting the impact of merchant rerouting and lower rates.

Transaction dollar volume decreased $862 million for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012, primarily driven by a reduction in Diners Club volume due to the impact of currency exchange rates, partially offset by an increase in Network Partners volume.

As previously disclosed, we have been working with our European Diners Club licensees with regard to their ability to maintain financing sufficient to support business operations. For example, we have provided loans to certain

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licensees that have an outstanding balance of approximately $36 million at December 31, 2013. We have undrawn commitments to lend these licensees up to an additional $19 million as of December 31, 2013, subject to collateral requirements stated in the individual agreements. During 2013, we acquired Diners Club Italy, which included $34 million of receivables, and we provided financial assistance to facilitate the purchase of our Slovenian licensee by a European bank. These transactions resulted in a charge to earnings of approximately $40 million in the second quarter of 2013. Additionally, we increased reserves by $15 million related to the loans to certain European Diners Club licensees, discussed above, due to liquidity concerns. There were no similar acquisitions, asset write downs or allowances in the prior year period.

Critical Accounting Estimates

In preparing our consolidated financial statements in conformity with accounting principles generally accepted in the United States ("GAAP"), management must make judgments and use estimates and assumptions about the effects of matters that are uncertain. For estimates that involve a high degree of judgment and subjectivity, it is possible that different estimates could reasonably be derived for the same period. For estimates that are particularly sensitive to changes in economic or market conditions, significant changes to the estimated amount from period to period are also possible. Management believes the current assumptions and other considerations used to estimate amounts reflected in our consolidated financial statements are appropriate. However, if actual experience differs from the assumptions and other considerations used in estimating amounts in our consolidated financial statements, the resulting changes could have a material effect on our consolidated results of operations and, in certain cases, could have a material effect on our consolidated financial condition. Management has identified the estimates related to our allowance for loan losses, the evaluation of goodwill and other non-amortizable intangible assets for potential impairment, the accrual of income taxes, and estimates of future cash flows associated with PCI loans as critical accounting estimates. Historically, management has considered the estimate of reward forfeitures to be a critical accounting estimate. In the fourth quarter of 2014, management made a series of changes to the redemption elements of our customer rewards program eliminating the forfeiture of rewards. These changes resulted in a one-time expense of $178 million due to the reversal of our current estimate for customer rewards forfeiture, a contra-liability account. With elimination of the forfeiture reward estimate, the determination of customer rewards cost no longer involves the use of a critical accounting estimate. See "— Other Income" and Note 2: Summary of Significant Accounting Policies to our consolidated financial statements for further details about customer rewards cost.

Allowance for Loan Losses

We base our allowance for loan losses on several analyses that help us estimate incurred losses as of the balance sheet date. This estimate considers uncollectible principal, interest and fees reflected in the loan receivables. While our estimation process includes historical data and analysis, there is a significant amount of judgment applied in selecting inputs and analyzing the results produced to determine the allowance. We use a migration analysis to estimate the likelihood that a loan will progress through the various stages of delinquency. Management also estimates loss emergence by using other analyses to estimate losses incurred from non-delinquent accounts. The considerations in these analyses include past and current loan performance, loan seasoning and growth, current risk management practices, account collection strategies, economic conditions, bankruptcy filings, policy changes and forecasting uncertainties. Given the same information, others may reach different reasonable estimates.

If management used different assumptions in estimating incurred net loan losses, the impact to the allowance for loan losses could have a material effect on our consolidated financial condition and results of operations. For example, a 10% change in management's estimate of incurred net loan losses could have resulted in a change of approximately $175 million in the allowance for loan losses at December 31, 2014, with a corresponding change in the provision for loan losses. See "— Loan Quality" and Note 2: Summary of Significant Accounting Policies to our consolidated financial statements for further details about our allowance for loan losses.

Goodwill

We recognize goodwill when the purchase price of an acquired business exceeds the total of the fair values of the acquired net assets. As required by GAAP, we test goodwill for impairment annually, or more often if indicators of impairment exist. In evaluating goodwill for impairment, management must estimate the fair value of the reporting unit(s) to which the goodwill relates. Because market data concerning acquisitions of comparable businesses typically

are not readily obtainable, other valuation techniques such as earnings multiples and cash flow models are used in estimating the fair values of these reporting units. In applying these techniques, management considers historical results, business forecasts, market and industry conditions and other factors. We may also consult independent valuation

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experts where needed in applying these valuation techniques. The valuation methodologies we use involve assumptions about business performance, revenue and expense growth, capital expenditures, discount rates and other assumptions that are judgmental in nature.

During the fourth quarter of 2013, we changed the date of its annual goodwill impairment test from June 1 to October 1. This goodwill impairment test date change was applied prospectively beginning on October 1, 2013 and had no effect on the consolidated financial statements.

At December 31, 2014, we had goodwill of $257 million. If economic conditions deteriorate or other events adversely impact the assumptions used by management in these valuations, we may be exposed to an impairment loss that, when recognized, could have a material impact on our consolidated financial condition and results of operations. At December 31, 2014, based on the annual impairment testing performed, there was the recognition of an impairment charge of $27 million related to the Discover Home Loans business. No other impairment was identified. See Note 7: Goodwill and Intangible Assets to our consolidated financial statements for further details about goodwill and the related impairment charge.

Other Non-amortizable Intangible Assets

We recognized certain other non-amortizable intangible assets in our acquisition of the Diners Club business. As required by GAAP, we test other non-amortizable intangible assets for impairment annually, or more often if indicators of impairment exist. Because market data concerning acquisitions of intangible assets is not readily available, management evaluates non-amortizable intangible assets for potential impairment by estimating their fair values using discounted cash flow models. In applying these techniques, management considers historical results, business forecasts, market and industry conditions and other factors. We may also consult independent valuation experts where needed in applying these valuation techniques. The valuation methodologies we use involve assumptions about business performance, revenue and expense growth, discount rates and other assumptions that are judgmental in nature.

During the fourth quarter of 2013, we changed the date of its annual impairment test for non-amortizable intangible assets from June 1 to October 1. No impairment charges were identified during the impairment tests conducted at June 1, 2013 and October 1, 2013.

At December 31, 2014, we had non-amortizable intangibles of $176 million. If economic conditions deteriorate or other events adversely impact the assumptions used by management in these valuations, we may be exposed to an impairment loss that, when recognized, could have a material impact on our consolidated financial condition and results of operations. At December 31, 2014, based on the annual impairment testing performed, there was no impairment recorded on any non-amortizable intangible asset.

Income Taxes

We are subject to the income tax laws of the jurisdictions where we have business operations, primarily the United States, its states and municipalities. We must make judgments and interpretations about the application of these inherently complex tax laws when determining the provision for income taxes and must also make estimates about when in the future certain items will affect taxable income in the various taxing jurisdictions. Disputes over interpretations of the tax laws may be settled with the taxing authority upon examination or audit. We regularly evaluate the likelihood of assessments in each of the taxing jurisdictions resulting from current and subsequent years' examinations, and tax reserves are established as appropriate.

Changes in the estimate of income taxes can occur due to tax rate changes, interpretations of tax laws, the status and resolution of examinations by the taxing authorities, and newly enacted laws and regulations that impact the relative merits of tax positions taken. When such changes occur, the effect on our consolidated financial condition and results of operations can be significant. See Note 15: Income Taxes to our consolidated financial statements for additional information about income taxes.

Purchased Credit-Impaired Loans

The estimate of expected future cash flows on purchased credit-impaired loans determines the amount of interest income we can recognize in future periods and impacts whether a loan loss reserve must be established for these loans. We reevaluate, by pool, the amount and timing of expected cash flows quarterly using updated loan portfolio characteristics as well as assumptions regarding expected borrower default and prepayment behavior. Because

estimates of expected future cash flows on PCI loans involve assumptions and significant judgment, it is reasonably

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possible that others could derive different estimates than ours for the same periods. In addition, changes in estimates from one period to the next can have a significant impact on our consolidated financial condition and results of operations. A decrease in expected cash flows involving an increase in estimated credit losses would result in an immediate charge to earnings for the recognition of a loan loss provision. Increases or decreases in expected cash flows related solely to changes in estimated prepayments or to changes in variable interest rate indices would result in prospective yield adjustments over the remaining life of the loans. An increase in expected cash flows due to a reduction in expected credit losses would result first in the reversal of any previously established loan loss reserve on PCI loans through an immediate credit to earnings and then, if needed, a prospective adjustment to yield over the remaining life of the loans.

If management used a different estimate of expected borrower defaults, our consolidated statement of financial condition and results of operations could have differed. For example, a 10% increase in the expected borrower default rate of each PCI loan pool as of December 31, 2014 could have resulted in an additional impairment of up to $11 million. This impairment would have been reflected as an increase in provision for loan losses and a decrease in the carrying value of the PCI loans. The accounting and estimates used in our calculations are discussed further in Note 4: Loan Receivables to our consolidated financial statements.

Earnings Summary

The following table outlines changes in our consolidated statements of income for the periods presented (dollars in millions):

	For the Calendar Years Ended December 31,		For the Fiscal Year Ended November 30, 2012	For the One Month Ended December 31, 2012	Calendar Year 2014 vs. Calendar Year 2013 increase (decrease)		Calendar Year 2013 vs. Fiscal Year 2012 increase (decrease)	
	2014	2013			$	%	$	%
Interest income	$7,596	$7,064	$6,703	$595	$532	8 %	$361	5 %
Interest expense	1,134	1,146	1,331	103	(12)	(1)%	(185)	(14)%
Net interest income	6,462	5,918	5,372	492	544	9 %	546	10 %
Provision for loan losses	1,443	1,086	848	178	357	33 %	238	28 %
Net interest income after provision for loan losses	5,019	4,832	4,524	314	187	4 %	308	7 %
Other income	2,015	2,306	2,281	200	(291)	(13)%	25	1 %
Other expense	3,340	3,194	3,052	240	146	5 %	142	5 %
Income before income tax expense	3,694	3,944	3,753	274	(250)	(6)%	191	5 %
Income tax expense	1,371	1,474	1,408	104	(103)	(7)%	66	5 %
Net income	$2,323	$2,470	$2,345	$170	$(147)	(6)%	$125	5 %

Net Interest Income

The tables that follow this section have been provided to supplement the discussion below and provide further analysis of net interest income, net interest margin and the impact of rate and volume changes on net interest income. Net interest income represents the difference between interest income earned on our interest-earning assets and the interest expense incurred to finance those assets. We analyze net interest income in total by calculating net interest margin (net interest income as a percentage of average total loan receivables) and net yield on interest-bearing assets (net interest income as a percentage of average total interest-earning assets). We also separately consider the impact of the level of loan receivables and the related interest yield and the impact of the cost of funds related to each of our funding sources, along with the income generated by our liquidity portfolio, on net interest income.

Our interest-earning assets consist of: (i) cash and cash equivalents, primarily related to amounts on deposit with the Federal Reserve, (ii) restricted cash, (iii) other short-term investments, (iv) investment securities and (v) loan

receivables. Our interest-bearing liabilities consist primarily of deposits, both direct-to-consumer and brokered, and long-term borrowings, including amounts owed to securitization investors. Net interest income is influenced by the following:

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- The level and composition of loan receivables, including the proportion of credit card loans to other loans, as well as the proportion of loan receivables bearing interest at promotional rates as compared to standard rates;
- The credit performance of our loans, particularly with regard to charge-offs of finance charges, which reduce interest income;
- The terms of long-term borrowings and certificates of deposit upon initial offering, including maturity and interest rate;
- The level and composition of other interest-bearing assets and liabilities, including our liquidity portfolio;
- Changes in the interest rate environment, including the levels of interest rates and the relationships among interest rate indices, such as the prime rate, the Federal Funds rate and the London Interbank Offered Rate ("LIBOR");
- The effectiveness of interest rate swaps in our interest rate risk management program; and
- The difference between the carrying amount and future cash flows expected to be collected on PCI loans.

For the Year Ended December 31, 2014 compared to the Year Ended December 31, 2013

Net interest margin increased for the year ended December 31, 2014 as compared to the year ended December 31, 2013 primarily driven by an increase in the yield on total loan receivables combined with lower interest rates on funding. The increase in loan receivable yields was driven by higher interest rates and growth in non-promotional revolving balances, partially offset by a decline in higher rate balances along with growth in credit card promotional balances.

Interest income increased during the year ended December 31, 2014 as compared to the year ended December 31, 2013 primarily due to higher average balances of credit card loans, personal loans and private student loans resulting from growth across these products. The increase was also attributable to higher yields on credit card loans and PCI student loans, partially offset by a decrease in yield on personal loans along with a decrease in PCI student loan balances.

Interest expense was relatively flat during the year ended December 31, 2014 as compared to the year ended December 31, 2013, as lower interest expense on deposits attributable to lower yields was offset by higher interest expense resulting from increase in borrowings.

For the Calendar Year Ended December 31, 2013 compared to the Fiscal Year Ended November 30, 2012

Net interest margin increased for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily driven by decreased funding costs and growth in loan receivables, partially offset by lower yields on loan receivables. The decrease in loan receivable yields was driven by growth in credit card promotional balances and a decline in higher rate balances, partially offset by growth in customers with revolving balances.

Interest income increased during the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily due to higher interest income from credit card loans, personal loans and private student loans resulting from growth across these products combined with lower credit card loan interest charge-offs. The increase in interest income from these products was partially offset by a decrease in yield on credit card loan receivables along with a decrease in PCI student loan balances.

Interest expense declined during the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily due to the combination of deposits bearing higher interest rates maturing and being replaced by deposits bearing lower interest rates and maturities of borrowings and certain asset-backed securities.

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Average Balance Sheet Analysis
(dollars in millions)

	Calendar Years Ended December 31, 2014			2013			Fiscal Year Ended November 30, 2012			One Month Ended December 31, 2012		
	Average Balance	Rate	Interest	Average Balance	Rate	Interest	Average Balance	Rate	Interest	Average Balance	Rate	Interest
Assets												
Interest-earning assets:												
Cash and cash equivalents	$7,228	0.25 %	$18	$5,557	0.25 %	$14	$5,074	0.27 %	$14	$2,704	0.25 %	$—
Restricted cash	763	0.08 %	1	704	0.10 %	1	924	0.15 %	2	1,400	0.11 %	—
Investment securities	4,000	1.67 %	67	5,190	1.42 %	74	6,437	1.24 %	80	6,247	1.34 %	7
Loan receivables[1]:												
Credit card[2][3]	52,600	12.09 %	6,359	49,816	12.00 %	5,978	47,301	12.16 %	5,751	50,494	11.92 %	510
Personal loans	4,592	12.36 %	568	3,706	12.52 %	464	2,944	12.35 %	363	3,290	12.43 %	35
Federal student loans[4]	—	NM	—	—	NM	—	121	1.64 %	2	—	NM	—
Private student loans	4,450	7.02 %	312	3,561	7.07 %	252	2,557	7.20 %	184	3,021	7.22 %	18
PCI student loans	3,916	6.64 %	260	4,434	6.13 %	272	4,998	6.06 %	303	4,724	5.96 %	24
Mortgage loans held for sale	118	3.92 %	5	216	3.47 %	7	96	1.10 %	1	310	3.05 %	1
Other	177	3.49 %	6	87	3.00 %	2	26	11.98 %	3	38	5.24 %	—
Total loan receivables	65,853	11.40 %	7,510	61,820	11.28 %	6,975	58,043	11.38 %	6,607	61,877	11.21 %	588
Total interest-earning assets	77,844	9.76 %	7,596	73,271	9.64 %	7,064	70,478	9.51 %	6,703	72,228	9.73 %	595
Allowance for loan losses	(1,645)			(1,639)			(1,948)			(1,725)		
Other assets	4,279			4,348			4,032			4,234		
Total assets	$80,478			$75,980			$72,562			$74,737		
Liabilities and Stockholders' Equity												
Interest-bearing liabilities:												
Interest-bearing deposits:												
Time deposits[5]	$26,627	1.66 %	443	$27,718	2.02 %	559	$27,033	2.61 %	706	$27,849	2.29 %	54
Money market deposits[6]	7,624	0.91 %	70	5,719	0.87 %	50	5,413	0.92 %	50	5,368	0.88 %	4
Other interest-bearing savings deposits	10,617	0.96 %	101	9,428	0.95 %	89	8,638	1.03 %	89	8,864	1.00 %	7

Total interest-bearing deposits[7]	44,868	1.37 %	614	42,865	1.63 %	698	41,084	2.06 %	845	42,081	1.84 %	65
Borrowings:												
Short-term borrowings	111	1.59 %	2	199	1.57 %	3	89	1.32 %	1	283	1.36 %	—
Securitized borrowings[5][6]	16,686	1.78 %	297	16,297	1.74 %	284	16,979	1.95 %	331	16,998	1.80 %	26
Other long-term borrowings[5]	4,192	5.28 %	221	2,609	6.18 %	161	2,017	7.62 %	154	1,733	7.82 %	12
Total borrowings	20,989	2.48 %	520	19,105	2.35 %	448	19,085	2.55 %	486	19,014	2.34 %	38
Total interest-bearing liabilities	65,857	1.72 %	1,134	61,970	1.85 %	1,146	60,169	2.21 %	1,331	61,095	1.99 %	103
Other liabilities and stockholders' equity	14,621			14,010			12,393			13,642		
Total liabilities and stockholders' equity	$80,478			$75,980			$72,562			$74,737		
Net interest income			$6,462			$5,918			$5,372			$492
Net interest margin[8]		9.81 %			9.57 %			9.25 %			9.39 %	
Net yield on interest-bearing assets[9]		8.30 %			8.08 %			7.62 %			8.05 %	
Interest rate spread[10]		8.04 %			7.79 %			7.30 %			7.74 %	

(1) Average balances of loan receivables include non-accruing loans, which are included in the yield calculations. If the non-accruing loan balances were excluded, there would not be a material impact on the amounts reported above.

(2) Interest income on credit card loans includes $192 million, $171 million, $179 million and $14 million of amortization of balance transfer fees for the calendar years ended December 31, 2014 and 2013, fiscal year ended November 30, 2012 and one month ended December 31, 2012, respectively.

(3) The calendar year ended December 31, 2013, fiscal year ended November 30, 2012 and one month ended December 31, 2012 include the impact of interest rate swap agreements used to change a portion of certain floating-rate credit card loan receivables to fixed-rate.

(4) Includes federal student loans held for sale.

(5) Includes the impact of interest rate swap agreements used to change a portion of fixed-rate funding to floating-rate funding.

(6) Includes the impact of interest rate swap agreements used to change a portion of floating-rate funding to fixed-rate funding.

(7) Includes the impact of FDIC insurance premiums.

(8) Net interest margin represents net interest income as a percentage of average total loan receivables.

(9)

Net yield on interest-bearing assets represents net interest income as a percentage of average total interest-earning assets.

(10) Interest rate spread represents the difference between the rate on total interest-earning assets and the rate on total interest-bearing liabilities.

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Rate/Volume Variance Analysis[1]
(dollars in millions)

	Calendar Year Ended December 31, 2014 vs. Calendar Year Ended December 31, 2013			Calendar Year Ended December 31, 2013 vs. Fiscal Year Ended November 30, 2012		
	Volume	Rate	Total	Volume	Rate	Total
Increase/(decrease) in net interest income due to changes in:						
Interest-earning assets:						
Cash and cash equivalents	$4	$—	$4	$1	$(1)	$—
Restricted cash	—	—	—	—	(1)	(1)
Investment securities	(19)	12	(7)	(17)	11	(6)
Loan receivables:						
Credit card	336	45	381	302	(75)	227
Personal loans	110	(6)	104	96	5	101
Federal student loans	—	—	—	(2)	—	(2)
Private student loans	62	(2)	60	71	(3)	68
PCI student loans	(33)	21	(12)	(34)	3	(31)
Mortgage loans held for sale	(3)	1	(2)	2	4	6
Other	3	1	4	3	(4)	(1)
Total loan receivables	475	60	535	438	(70)	368
Total interest income	460	72	532	422	(61)	361
Interest-bearing liabilities:						
Interest-bearing deposits:						
Time deposits	(21)	(95)	(116)	18	(165)	(147)
Money market deposits	17	3	20	3	(3)	—
Other interest-bearing savings deposits	11	1	12	8	(8)	—
Total interest-bearing deposits	7	(91)	(84)	29	(176)	(147)
Borrowings:						
Short-term borrowings	(1)	—	(1)	2	—	2
Securitized borrowings	7	6	13	(13)	(34)	(47)
Other long-term borrowings	86	(26)	60	40	(33)	7
Total borrowings	92	(20)	72	29	(67)	(38)
Total interest expense	99	(111)	(12)	58	(243)	(185)
Net interest income	$361	$183	$544	$364	$182	$546

(1) The rate/volume variance for each category has been allocated on a consistent basis between rate and volume variances between the calendar years ended December 31, 2014 and 2013, and fiscal year ended November 30, 2012 based on the percentage of the rate or volume variance to the sum of the two absolute variances.

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Loan Quality

Loan receivables consist of the following (dollars in millions):

	December 31,			November 30,		
	2014	2013	2012	2012	2011	2010
Student loans held for sale	$—	$—	$—	$—	$714	$788
Loan portfolio:						
Credit card loans	56,128	53,150	51,135	49,642	46,972	45,502
Other loans:						
Personal loans	5,007	4,191	3,296	3,272	2,648	1,878
Private student loans	4,850	3,969	3,072	3,000	2,069	999
Mortgage loans held for sale	122	148	355	322	—	—
Other	202	135	38	37	17	14
Total other loans	10,181	8,443	6,761	6,631	4,734	2,891
PCI loans[1]	3,660	4,178	4,702	4,744	5,250	—
Total loan portfolio	69,969	65,771	62,598	61,017	56,956	48,393
Total loan receivables	69,969	65,771	62,598	61,017	57,670	49,181
Allowance for loan losses	(1,746)	(1,648)	(1,788)	(1,725)	(2,205)	(3,304)
Net loan receivables	$68,223	$64,123	$60,810	$59,292	$55,465	$45,877

(1) Represents purchased credit-impaired private student loans (see Note 4: Loan Receivables to our consolidated financial statements).

Provision and Allowance for Loan Losses

Provision for loan losses is the expense related to maintaining the allowance for loan losses at an appropriate level to absorb the estimated probable losses in the loan portfolio at each period end date. Factors that influence the provision for loan losses include:

- The impact of general economic conditions on the consumer, including unemployment levels, bankruptcy trends and interest rate movements;
- Changes in consumer spending and payment behaviors;
- Changes in our loan portfolio, including the overall mix of accounts, products and loan balances within the portfolio and maturation of the loan portfolio;
- The level and direction of historical and anticipated loan delinquencies and charge-offs;
- The credit quality of the loan portfolio, which reflects, among other factors, our credit granting practices and effectiveness of collection efforts; and
- Regulatory changes or new regulatory guidance.

In calculating the allowance for loan losses, we estimate probable losses separately for segments of the loan portfolio that have similar risk characteristics. We use a migration analysis to estimate the likelihood that a loan will progress through the various stages of delinquency. We use other analyses to estimate losses incurred from non-delinquent accounts which adds to the identification of loss emergence. We use these analyses together as a basis for determining our allowance for loan losses.

The allowance for loan losses was $1.7 billion at December 31, 2014, which reflects a $98 million reserve build over the amount of the allowance for loan losses at December 31, 2013. The reserve build, which primarily related to credit card loan receivables, was due mainly to seasoning of the loan growth and lower recoveries. "Seasoning" refers to the maturing of a loan portfolio as, in general, growing loan balances do not begin to show signs of credit deterioration or default until they have been in repayment for some period of time. At December 31, 2013, the allowance for loan losses was $1.6 billion, which reflected a $140 million reserve release over the amount of the allowance for loan losses at December 31, 2012. The reserve release, which primarily related to credit card loan receivables, was driven by continuing favorability in delinquencies resulting in lower charge-offs, both contractual and bankruptcy, which resulted in lower estimated losses.

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The provision for loan losses is the amount of expense realized after considering the level of net charge-offs in the period and the required amount of allowance for loan losses at the balance sheet date. For the year ended December 31, 2014, the provision for loan losses increased by $357 million, or 33%, as compared to the year ended December 31, 2013. The increase was primarily due to increasing levels of net charge-offs combined with the reserve build discussed above. For the calendar year ended December 31, 2013, the provision for loan losses increased by $238 million, or 28%, as compared to the fiscal year ended November 30, 2012. The increase was due to lower levels of reserve releases during the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012, partially offset by a decrease in net charge-offs. For the one month ended December 31, 2012, the provision for loan losses was $178 million, which included a reserve build of $63 million. This reserve build was due to an increase in the forecast for net charge-offs due to loan growth. For the fiscal year ended November 30, 2012, a reduction in reserve requirements led to a decrease in the provisions for loan losses of $165 million or 16%.
At December 31, 2014, the level of the allowance related to personal loans and student loans increased as compared to December 31, 2013 due to loan growth and continued seasoning of the portfolios. For student loans, payments are not required while the borrower is still in school; therefore, this loan portfolio matures at a slower pace than our other loan portfolios. The level of allowance related to other loans was unchanged for the period.

At December 31, 2013, the level of the allowance related to personal loans increased as compared to December 31, 2012 due to loan growth and continued seasoning of the portfolio. The level of allowance attributable to student loans for the same period increased, primarily due to a PCI student loan impairment recorded as a result of revisions to credit loss assumptions for the underlying loans. In addition, the allowance related to student loans increased due to growth and continued seasoning of the portfolio. The level of allowance related to other loans at December 31, 2013 as compared to December 31, 2012 increased by $16 million driven primarily by provision charges on a small number of loans to Diners Club licensees.

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The following tables provide changes in our allowance for loan losses for the periods presented (dollars in millions):

	For the Calendar Year Ended December 31, 2014				
	Credit Card	Personal Loans	Student Loans	Other	Total
Balance at beginning of period	$1,406	$112	$113	$17	$1,648
Additions:					
Provision for loan losses	1,259	102	79	3	1,443
Deductions:					
Charge-offs	(1,636)	(105)	(62)	(3)	(1,806)
Recoveries	445	11	5	—	461
Net charge-offs	(1,191)	(94)	(57)	(3)	(1,345)
Balance at end of period	$1,474	$120	$135	$17	$1,746

	For the Calendar Year Ended December 31, 2013				
	Credit Card	Personal Loans	Student Loans	Other	Total
Balance at beginning of period	$1,613	$99	$75	$1	$1,788
Additions:					
Provision for loan losses	893	92	84	17	1,086
Deductions:					
Charge-offs	(1,604)	(86)	(48)	(1)	(1,739)
Recoveries	504	7	2	—	513
Net charge-offs	(1,100)	(79)	(46)	(1)	(1,226)
Balance at end of period	$1,406	$112	$113	$17	$1,648

	For the One Month Ended December 31, 2012				
	Credit Card	Personal Loans	Student Loans	Other	Total
Balance at beginning of period	$1,554	$97	$73	$1	$1,725
Additions:					
Provision for loan losses	165	9	4	—	178
Deductions:					
Charge-offs	(146)	(8)	(2)	—	(156)
Recoveries	40	1	—	—	41
Net charge-offs	(106)	(7)	(2)	—	(115)
Balance at end of period	$1,613	$99	$75	$1	$1,788

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The following tables provide changes in our allowance for loan losses for the periods presented (dollars in millions):

	For the Fiscal Year Ended November 30, 2012				
	Credit Card	Personal Loans	Student Loans	Other	Total
Balance at beginning of period	$2,070	$82	$53	$—	$2,205
Additions:					
Provision for loan losses	724	84	39	1	848
Deductions:					
Charge-offs	(1,817)	(73)	(19)	—	(1,909)
Recoveries	577	4	—	—	581
Net charge-offs	(1,240)	(69)	(19)	—	(1,328)
Balance at end of period	$1,554	$97	$73	$1	$1,725

	For the Fiscal Year Ended November 30, 2011				
	Credit Card	Personal Loans	Student Loans	Other	Total
Balance at beginning of period	$3,209	$76	$18	$1	$3,304
Additions:					
Provision for loan losses	897	73	42	1	1,013
Deductions:					
Charge-offs	(2,615)	(69)	(7)	(2)	(2,693)
Recoveries	579	2	—	—	581
Net charge-offs	(2,036)	(67)	(7)	(2)	(2,112)
Balance at end of period	$2,070	$82	$53	$—	$2,205

	For the Fiscal Year Ended November 30, 2010				
	Credit Card	Personal Loans	Student Loans	Other	Total
Balance at beginning of period	$1,648	$95	$14	$1	$1,758
Additions:					
Addition to allowance related to securitized receivables[1]	2,144	—	—	—	2,144
Provision for loan losses	3,126	72	8	1	3,207
Deductions:					
Charge-offs related to loans sold	(25)	—	—	—	(25)
Charge-offs	(4,154)	(92)	(4)	(1)	(4,251)
Recoveries	470	1	—	—	471
Net charge-offs	(3,684)	(91)	(4)	(1)	(3,780)
Balance at end of period	$3,209	$76	$18	$1	$3,304

(1) On December 1, 2009, upon adoption of the Financial Accounting Standards Board ("FASB") Statements No. 166 and 167, we recorded $2.1 billion allowance for loan losses related to newly consolidated and reclassified credit card loan receivables.

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Net Charge-offs

Our net charge-offs include the principal amount of losses charged off less principal recoveries and exclude charged-off and recovered interest and fees and fraud losses. Charged-off and recovered interest and fees are recorded in interest income and loan fee income, respectively, which is effectively a reclassification of the provision for loan losses, while fraud losses are recorded in other expense. Credit card loan receivables are charged off at the end of the month during which an account becomes 180 days contractually past due. Personal loans and private student loans, which are closed-end consumer loan receivables, are generally charged off at the end of the month during which an account becomes 120 days contractually past due. Generally, customer bankruptcies and probate accounts are charged off at the end of the month 60 days following the receipt of notification of the bankruptcy or death but not later than the 180-day or 120-day contractual time frame.

The following table presents amounts and rates of net charge-offs of key loan products (dollars in millions):

	For the Calendar Years Ended December 31,				For the Fiscal Years Ended November 30,						For the One Month Ended December 31, 2012	
	2014		2013		2012		2011		2010			
	$	%	$	%	$	%	$	%	$	%	$	%
Credit card loans	$1,191	2.27 %	$1,100	2.21 %	$1,240	2.62 %	$2,036	4.47 %	$3,684	8.02 %	$106	2.47 %
Personal loans	$94	2.04 %	$79	2.13 %	$69	2.33 %	$67	3.02 %	$91	5.72 %	$7	2.52 %
Private student loans (excluding PCI[(1)])	$57	1.29 %	$46	1.30 %	$19	0.73 %	$7	0.48 %	$4	0.33 %	$2	0.81 %

(1) Charge-offs for PCI loans did not result in a charge to earnings during any of the years presented and are therefore excluded from the calculation. See Note 4: Loan Receivables to our consolidated financial statements for more information regarding the accounting for charge-offs on PCI loans.

While the net charge-off rate on our credit card loan receivables went to 2.27% from 2.21% for the year ended December 31, 2014 as compared to the year ended December 31, 2013, we remain in a period of historical lows. The net charge-off rate on our personal loan receivables declined by 9 basis points for the same period due to growth in the personal loan portfolio as, in general, loans do not begin to show signs of credit deterioration or default for some period of time after origination. The net charge-off rate on our private student loans excluding PCI loans was relatively flat for the year ended December 31, 2014 as compared to year ended December 31, 2013.

The net charge-off rate on our credit card loan receivables decreased 41 basis points for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012. The decrease in the net charge-off rate for credit card loan receivables was driven by lower net charge-offs due to the continuing trend of low delinquencies combined with higher receivables balances. The net charge-off rate on our personal loan receivables declined by 20 basis points for the same period due to growth in the personal loan portfolio. The net charge-off rate on our private student loans excluding PCI loans increased 57 basis points due to a larger portion of the portfolio entering repayment.

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Delinquencies

Delinquencies are an indicator of credit quality at a point in time. A loan balance is considered delinquent when contractual payments on the loan become 30 days past due.

The following table presents the amounts and delinquency rates of key loan products that are 30 and 90 days or more delinquent, loan receivables that are not accruing interest, regardless of delinquency and restructured loans (dollars in millions):

	Calendar Years Ended December 31,				Fiscal Years Ended November 30,						One Month Ended December 31, 2012	
	2014		2013		2012		2011		2010			
	$	%	$	%	$	%	$	%	$	%	$	%
Loans 30 days delinquent or more:												
Credit card loans	$971	1.73 %	$912	1.72 %	$925	1.86 %	$1,117	2.38 %	$1,831	4.02 %	$917	1.79 %
Personal loans	$40	0.79 %	$29	0.70 %	$25	0.76 %	$22	0.87 %	$29	1.57 %	$26	0.77 %
Private student loans (excluding PCI[1])	$87	1.80 %	$66	1.66 %	$32	1.07 %	$13	0.63 %	$5	0.50 %	$37	1.22 %
Loans 90 days delinquent or more:												
Credit card loans	$480	0.85 %	$447	0.84 %	$451	0.91 %	$560	1.19 %	$958	2.11 %	$460	0.90 %
Personal loans	$11	0.22 %	$8	0.21 %	$8	0.23 %	$7	0.28 %	$11	0.57 %	$8	0.23 %
Private student loans (excluding PCI[1])	$25	0.52 %	$18	0.46 %	$8	0.27 %	$3	0.14 %	$1	0.14 %	$9	0.29 %
Loans not accruing interest	$183	0.28 %	$200	0.33 %	$198	0.35 %	$207	0.40 %	$326	0.67 %	$192	0.33 %
Restructured loans:												
Credit card loans[2]	$1,037	1.85 %	$1,123	2.11 %	$1,332	2.68 %	$1,217	2.59 %	$305	0.67 %	$1,309	2.56 %
Personal loans[3]	$55	1.10 %	$31	0.74 %	$21	0.64 %	$8	0.29 %	$—	— %	$21	0.65 %
Private student loans(excluding PCI[1])[4]	$38	0.78 %	$28	0.71 %	$15	0.50 %	$5	0.26 %	$—	— %	$16	0.53 %

(1) Excludes PCI loans which are accounted for on a pooled basis. Since a pool is accounted for as a single asset with a single composite interest rate and aggregate expectation of cash flows, the past-due status of a pool, or that of the individual loans within a pool, is not meaningful. Because we are recognizing interest income on a pool of loans, it is all considered to be performing.

(2) Restructured loans include $44 million, $43 million, $54 million, $56 million, $38 million and $35 million at December 31, 2014, 2013 and 2012 and November 30, 2012, 2011 and 2010, respectively, that are also included in loans over 90 days delinquent or more.

(3)

Restructured loans include $3 million, $2 million, $2 million and $1 million at December 31, 2014, 2013 and 2012 and November 30, 2012 respectively, that are also included in loans over 90 days delinquent or more.

(4) Restructured loans include $5 million, $3 million, $2 million and $2 million at December 31, 2014, 2013 and 2012 and November 30, 2012 respectively, that are also included in loans over 90 days delinquent or more.

Credit card receivables 30-day and 90-day delinquency rates at December 31, 2014 were relatively flat as compared to December 31, 2013. The 30-day delinquency rate for personal loans increased slightly for the same period due to seasoning of the loan portfolio, while the 90-day delinquency rate remained relatively flat. The 30-day and 90-day delinquency rates for private student loan balances at December 31, 2014 increased compared to the prior year as a result of continued seasoning of the student loan portfolio.

Both credit card and personal loan receivables 30-day and 90-day delinquency rates at December 31, 2013 decreased slightly as compared to December 31, 2012 due to continuing favorable economic factors. The delinquency rates for private student loan balances at December 31, 2013 increased as compared to December 31, 2012 due to the seasoning of our loan portfolio as more loans have entered repayment.

The restructured credit card loan balance decreased at both December 31, 2014 as compared to December 31, 2013 and at December 31, 2013 as compared December 31, 2012 due to continued improvement in customer credit performance. The restructured personal and private student loan balances increased at both December 31, 2014 as

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compared to December 31, 2013 and at December 31, 2013 as compared to December 31, 2012 as a result of continued growth in and seasoning of these loan portfolios.

Maturities and Sensitivities of Loan Receivables to Changes in Interest Rates

Our loan portfolio had the following maturity distribution[1] (dollars in millions):

	Due One Year or Less	Due After One Year Through Five Years	Due After Five Years	Total
At December 31, 2014				
Credit card loans	$16,253	$29,715	$10,160	$56,128
Personal loans	1,352	3,505	150	5,007
Private student loans (excluding PCI)	110	949	3,791	4,850
PCI loans	310	1,234	2,116	3,660
Mortgage loans held for sale	122	—	—	122
Other loans	27	56	119	202
Total loan portfolio	$18,174	$35,459	$16,336	$69,969

(1) Because of the uncertainty regarding loan repayment patterns, the above amounts have been calculated using contractually required minimum payments. Historically, actual loan repayments have been higher than such minimum payments and, therefore, the above amounts may not necessarily be indicative of our actual loan repayments.

At December 31, 2014, approximately $35.0 billion of our loan portfolio due after one year had interest rates tied to an index and approximately $16.8 billion were fixed-rate loans.

Modified and Restructured Loans

We have loan modification programs that provide for temporary or permanent hardship relief for our credit card loans to borrowers experiencing financial difficulties. The temporary hardship program primarily consists of a reduced minimum payment and an interest rate reduction, both lasting for a period no longer than 12 months. The permanent modification program involves changing the structure of the loan to a fixed payment loan with a maturity no longer than 60 months and reducing the interest rate on the loan. The permanent modification program does not normally provide for the forgiveness of unpaid principal, but may allow for the reversal of certain unpaid interest or fee assessments. We also make loan modifications for customers who request financial assistance through external sources, such as a consumer credit counseling agency program. These loans continue to be subject to the original minimum payment terms and do not normally include waiver of unpaid principal, interest or fees. For additional information regarding the accounting treatment for these loans as well as amounts recorded in the financial statements related to these loans, see Note 4: Loan Receivables to our consolidated financial statements.

For student loan borrowers, in certain situations we offer hardship payment forbearance to borrowers who are experiencing temporary financial difficulties and are willing to resume making payments. When a borrower is 30 or more days delinquent and granted a second hardship forbearance period, we classify these loans as troubled debt restructurings. In addition, we offer temporary reduced payment programs, which normally consist of a reduction of the minimum payment for a period of no longer than 12 months at a time. When a student loan borrower is enrolled in a temporary reduced payment program for 12 months or fewer over the life of the loan, the modification is not considered a troubled debt restructuring. No loans have been in a temporary modification program for greater than 12 months.

For personal loan customers, in certain situations we offer various payment programs, including temporary and permanent programs. The temporary programs normally consist of a reduction of the minimum payment for a period of no longer than 12 months with the option of a final balloon payment required at the end of the loan term or an extension of the maturity date with the total term not exceeding nine years. Further, in certain circumstances, the interest rate on the loan is reduced. The permanent programs involve changing the terms of the loan in order to pay off the outstanding balance over a longer term and also in certain circumstances reducing the interest rate on the loan.

Similar to the temporary programs, the total term may not exceed nine years. We also allow loan modifications for customers who request financial assistance through external sources, similar to our credit card customers discussed above. Payments are modified based on the new terms agreed upon with the credit counseling agency. Personal loans included

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in temporary and permanent programs are accounted for as troubled debt restructurings. Beginning in first quarter of 2014, loan modifications through external sources are accounted for as troubled debt restructurings.
Borrower performance after using payment programs or forbearance is monitored and we believe the programs help to prevent defaults and are useful in assisting customers experiencing financial difficulties. We plan to continue to use payment programs and forbearance and, as a result, we expect to have additional loans classified as troubled debt restructurings in the future.

Other Income

The following table presents the components of other income for the periods presented (dollars in millions):

	For the Calendar Years Ended December 31,		For the Fiscal Year Ended November 30, 2012	For the One Month Ended December 31, 2012	2014 Calendar Year vs. 2013 Calendar Year (decrease) increase		2013 Calendar Year vs. 2012 Fiscal Year increase (decrease)	
	2014	2013			$	%	$	%
Discount and interchange revenue[1]	$979	$1,126	$1,035	$82	$(147)	(13)%	$91	9%
Protection products	314	350	409	33	(36)	(10)%	(59)	(14)%
Loan fee income	334	320	325	29	14	4%	(5)	(2)%
Transaction processing revenue	182	192	218	18	(10)	(5)%	(26)	(12)%
Gain on investments	4	5	26	2	(1)	(20)%	(21)	(81)%
Gain on origination and sale of mortgage loans	81	144	105	17	(63)	(44)%	39	37%
Other income	121	169	163	19	(48)	(28)%	6	4%
Total other income	$2,015	$2,306	$2,281	$200	$(291)	(13)%	$25	1%

(1) Net of rewards, including Cashback Bonus rewards, of $1.4 billion, $1.0 billion, $1.0 billion and $123 million for the calendar years ended December 31, 2014 and 2013, fiscal year ended November 30, 2012 and one month ended December 31, 2012, respectively. During the three months ended December 31, 2014, we made certain changes to its customer rewards program, eliminating forfeitures. These changes resulted in a one-time expense of $178 million due to the reversal of the estimate for customer rewards forfeiture, a contra-account to accrued expenses and other liabilities. Actual forfeitures resulted in additional discount and interchange revenue and total other income of $36 million each for the calendar years ended December 31, 2014 and 2013 and $35 million and $3 million for the fiscal year ended November 30, 2012 and one month ended December 31, 2012, respectively.

Discount and Interchange Revenue

Discount and interchange revenue includes discount revenue and acquirer interchange net of interchange paid to network partners. We earn discount revenue from fees charged to merchants with whom we have entered into card acceptance agreements for processing credit card purchase transactions. We earn acquirer interchange revenue from merchant acquirers on all Discover Network card transactions and certain Diners Club transactions made by credit card customers at merchants with whom merchant acquirers have entered into card acceptance agreements for processing credit card purchase transactions. We incur an interchange cost to card issuing entities that have entered into contractual arrangements to issue cards on the Discover Network and on certain transactions on the Diners Club network. This cost is contractually established and is based on the card issuing organization's transaction volume and is reported as a reduction to discount and interchange revenue. We offer our customers various reward programs, including the Cashback Bonus reward program, pursuant to which we pay certain customers a percentage of their purchase amounts based on the type and volume of the customer's purchases. Reward costs are recorded as a reduction to discount and interchange revenue.

Discount and interchange revenue decreased for the year ended December 31, 2014 as compared to the year ended December 31, 2013, driven primarily by the rewards redemption policy change. This increase in rewards was partially offset by the increase in gross discount and interchange revenue, which was primarily attributable to higher sales volume. Discount and interchange revenue increased for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012, driven by higher sales volume.

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Protection Products

We earn revenue related to fees received for providing ancillary products and services, including payment protection and identity theft protection services, to customers. The amount of revenue recorded is generally based on either a percentage of a customer's outstanding balance or a flat fee and is recognized as earned.

Protection product revenue decreased for the year ended December 31, 2014 as compared to the year ended December 31, 2013, as well as for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012. The decrease in protection product revenue reflects lower sales volume as we have stopped selling these products.

Loan Fee Income

Loan fee income consists primarily of fees on credit card loans and includes late, cash advance and other miscellaneous fees. Loan fee income increased slightly as compared to the year ended December 31, 2013 primarily due to higher late fees and cash advance fees. Loan fee income decreased slightly for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012 primarily due to lower volume of loan fees being generated, partially offset by fewer late fee charge-offs as a result of decrease in credit card delinquency rates.

Transaction Processing Revenue

Transaction processing revenue represents switch fees charged to financial institutions and merchants for processing ATM, debit and point-of-sale transactions over the PULSE network, as well as various participation and membership fees. Switch fees are charged on a per transaction basis. Transaction processing revenue decreased both for the year ended December 31, 2014 as compared to the year ended December 31, 2013, and for the calendar year ended December 31, 2013, as compared to the fiscal year ended November 30, 2012, reflecting the impact of merchant rerouting and lower rates.

Gain on Investments

Gain on investments includes net realized gains on the sale of investments, net of any write-downs of investment securities to fair value when the decline in fair value is considered other than temporary. Gain on investments for the years ended December 31, 2014 and 2013 was mainly comprised of gains on the sales of U.S. Treasury and Agency Securities. Gain on investment securities for the fiscal year ended November 30, 2012 was comprised almost entirely of a gain of $26 million related to the liquidation of a minority interest in an equity investment.

Gain on Origination and Sale of Mortgage Loans

Gain on sale of mortgage loans consists of the net gain on the origination and sale of loans as well as the net gain on the related interest rate lock commitments and the net gain or loss on forward delivery contracts. Revenue related to mortgage banking operations declined for the year ended December 31, 2014 as compared to the year ended December 31, 2013 primarily driven by an increase in mortgage interest rates that resulted in lower mortgage refinance volume. Decline in revenue related to mortgage banking operation was also due to reduced margins in the industry resulting from increased competitive pressure since the increase in mortgage rates. Gain on sale of mortgage loans increased for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012, due to a full year of activity for the calendar year ended December 31, 2013 as compared to only a partial year of activity for the fiscal year ended November 30, 2012. The increase was partially offset by decrease in refinance mortgage loan volume due to increasing interest rates during 2013. The partial year of activity for the fiscal year ended November 30, 2012 resulted from the acquisition and integration of the assets of Home Loan Center in June of 2012.

Other Income

Other income includes royalty revenues earned by Diners Club, merchant fees, revenue from the transition services agreement related to the acquisition of SLC, revenue from merchants related to reward programs, revenues from network partners and other miscellaneous revenue items.

Other income decreased for the year ended December 31, 2014 as compared to the year ended December 31, 2013 primarily due to certain merchant network fees that were reclassified out of other income to discount and interchange revenue during 2014. Other income was relatively flat for the calendar year ended December 31, 2013 as compared to the fiscal year ended November 30, 2012.

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Other Expense

The following table represents the components of other expense for the periods presented (dollars in millions):

	For the Calendar Years Ended December 31,		For the Fiscal Year Ended November 30, 2012	For the One Month Ended December 31, 2012	2014 Calendar Year vs. 2013 Calendar Year increase (decrease)		2013 Calendar Year vs. 2012 Fiscal Year increase (decrease)	
	2014	2013			$	%	$	%
Employee compensation and benefits	$1,242	$1,164	$1,048	$87	$78	7 %	$116	11 %
Marketing and business development	735	717	603	51	18	3 %	114	19 %
Information processing and communications	346	333	289	25	13	4 %	44	15 %
Professional fees	450	410	432	34	40	10 %	(22)	(5)%
Premises and equipment	92	82	76	8	10	12 %	6	8 %
Other expense	475	488	604	35	(13)	(3)%	(116)	(19)%