STATE STREET CORP
Form 10-Q
November 06, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
Form 10-Q

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

For the quarterly period ended September 30, 2015

OR

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

For the transition period from to

Commission File No. 001-07511

STATE STREET CORPORATION
(Exact name of registrant as specified in its charter)

Massachusetts	04-2456637
(State or other jurisdiction of incorporation)	(I.R.S. Employer Identification No.)
One Lincoln Street Boston, Massachusetts	02111
(Address of principal executive office)	(Zip Code)

617-786-3000
(Registrant's telephone number, including area code)

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

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

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

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

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

The number of shares of the registrant's common stock outstanding as of October 31, 2015 was 403,486,112.

STATE STREET CORPORATION
QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTERLY PERIOD ENDED
SEPTEMBER 30, 2015

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MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

State Street Corporation, referred to as the parent company, is a financial holding company organized in 1969 under the laws of the Commonwealth of Massachusetts. Our executive offices are located at One Lincoln Street, Boston, Massachusetts 02111 (telephone (617) 786-3000). For purposes of this Form 10-Q, unless the context requires otherwise, references to “State Street,” “we,” “us,” “our” or similar terms mean State Street Corporation and its subsidiaries on a consolidated basis. The parent company is a source of financial and managerial support to our subsidiaries. Through our subsidiaries, including our principal banking subsidiary, State Street Bank and Trust Company, referred to as State Street Bank, we provide a broad range of financial products and services to institutional investors worldwide.

As of September 30, 2015, we had consolidated total assets of $247.27 billion, consolidated total deposits of $186.37 billion, consolidated total shareholders' equity of $21.50 billion and 31,860 employees. We operate in more than 100 geographic markets worldwide, including in the U.S., Canada, Europe, the Middle East and Asia. We are a leader in providing financial services and products to meet the needs of institutional investors worldwide, with $27.27 trillion of assets under custody and administration and $2.20 trillion of assets under management as of September 30, 2015.

We have two lines of business:

Investment Servicing provides services for institutional clients, including mutual funds, collective investment funds and other investment pools, corporate and public retirement plans, insurance companies, foundations and endowments worldwide. Products include custody; product- and participant-level accounting; daily pricing and administration; master trust and master custody; record-keeping; cash management; foreign exchange, brokerage and other trading services; securities finance; deposit and short-term investment facilities; loans and lease financing; investment manager and alternative investment manager operations outsourcing; and performance, risk and compliance analytics to support institutional investors.

Investment Management, through State Street Global Advisors, or SSGA, provides a broad array of investment management, investment research and investment advisory services to corporations, public funds and other sophisticated investors. SSGA offers active and passive asset management strategies across equity, fixed-income and cash asset classes. Products are distributed directly and through intermediaries using a variety of investment vehicles, including exchange-traded funds, or ETFs, such as the SPDR® ETF brand.

For financial and other information about our lines of business, refer to “Line of Business Information” included in this Management's Discussion and Analysis and note 17 to the consolidated financial statements included in this Form 10-Q.

This Management's Discussion and Analysis is part of our Quarterly Report on Form 10-Q for the quarter ended September 30, 2015, and updates the Management's Discussion and Analysis in our Annual Report on Form 10-K for the year ended December 31, 2014, which we refer to as the 2014 Form 10-K, previously filed with the Securities and Exchange Commission, or SEC. You should read the financial information contained in this Management's Discussion and Analysis and elsewhere in this Form 10-Q in conjunction with the financial and other information contained in our 2014 Form 10-K. Certain previously reported amounts presented in this Form 10-Q have been reclassified to conform to current-period presentation.

We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the U.S., referred to as GAAP. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions in its application of certain accounting policies that materially affect the reported amounts of assets, liabilities, equity, revenue and expenses.

The significant accounting policies that require us to make judgments, estimates and assumptions that are difficult, subjective or complex about matters that are uncertain and may change in subsequent periods include accounting for fair value measurements; other-than-temporary impairment of investment securities; impairment of goodwill and other intangible assets; and contingencies. These significant accounting policies require the most subjective or complex judgments, and underlying estimates and assumptions could be subject to revision as new information becomes available. Additional information about these significant accounting policies is included under “Significant Accounting Estimates” in Management's Discussion and Analysis in our 2014 Form 10-K. We did not change these significant accounting policies in the first nine months of 2015.

Certain financial information provided in this Form 10-Q, including this Management's Discussion and Analysis, is prepared on both a GAAP, or reported basis, and a non-GAAP, or operating basis, including certain non-GAAP measures used in the

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calculation of identified regulatory capital ratios. We measure and compare certain financial information on an operating basis, as we believe that this presentation supports meaningful comparisons from period to period and the analysis of comparable financial trends with respect to State Street's normal ongoing business operations. We believe that operating-basis financial information, which reports non-taxable revenue, such as interest revenue associated with tax-exempt investment securities, on a fully taxable-equivalent basis, facilitates an investor's understanding and analysis of State Street's underlying financial performance and trends in addition to financial information prepared and reported in conformity with GAAP. We also believe that the use of certain non-GAAP measures in the calculation of identified regulatory capital ratios is useful in understanding State Street's capital position and is of interest to investors.

Operating-basis financial information should be considered in addition to, not as a substitute for or superior to, financial information prepared in conformity with GAAP. Any non-GAAP, or operating-basis, financial information presented in this Form 10-Q, including this Management's Discussion and Analysis, is reconciled to its most directly comparable GAAP-basis measure.

We provide additional disclosures required by applicable bank regulatory standards, including supplemental qualitative and quantitative information with respect to regulatory capital (including market risk associated with our trading activities), summary results of semi-annual State Street-run stress tests which we conduct under the Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Dodd-Frank Act, and resolution plan disclosures required under the Dodd-Frank Act. These additional disclosures are accessible on the "Investor Relations" section of our corporate website at www.statestreet.com.

We have included our website address in this report as an inactive textual reference only. Information on our website is not incorporated by reference into this Form 10-Q.

Forward-Looking Statements

This Form 10-Q, as well as other reports submitted by us under the Securities Exchange Act of 1934, registration statements filed by us under the Securities Act of 1933, our annual report to shareholders and other public statements we may make, contain statements (including statements in the Management's Discussion and Analysis) that are considered "forward-looking statements" within the meaning of U.S. securities laws, including statements about our goals and expectations regarding our business, financial and capital condition, results of operations, strategies, financial portfolio performance, dividend and stock purchase programs, expected outcomes of legal proceedings, market growth, acquisitions, joint ventures and divestitures and new technologies, services and opportunities, as well as regarding industry, regulatory, economic and market trends, initiatives and developments, the business environment and other matters.

Terminology such as "plan," "expect," "intend," "objective," "forecast," "outlook," "believe," "anticipate," "estimate," "seek," "trend," "target," "strategy" and "goal," or similar statements or variations of such terms, are intended to identify forward-looking statements, although not all forward-looking statements contain such terms.

Forward-looking statements are subject to various risks and uncertainties, which change over time, are based on management's expectations and assumptions at the time the statements are made, and are not guarantees of future results. Management's expectations and assumptions, and the continued validity of the forward-looking statements, are subject to change due to a broad range of factors affecting the national and global economies, regulatory environment and the equity, debt, currency and other financial markets, as well as factors specific to State Street and its subsidiaries, including State Street Bank. Factors that could cause changes in the expectations or assumptions on which forward-looking statements are based cannot be foreseen with certainty and include, but are not limited to:

- the financial strength and continuing viability of the counterparties with which we or our clients do business and to which we have investment, credit or financial exposure, including, for example, the direct and indirect effects on counterparties of the sovereign-debt risks in the U.S., Europe and other regions;
- increases in the volatility of, or declines in the level of, our net interest revenue, changes in the composition or valuation of the assets recorded in our consolidated statement of condition (and our ability to measure the fair value of

investment securities) and the possibility that we may change the manner in which we fund those assets;

- the liquidity of the U.S. and international securities markets, particularly the markets for fixed-income securities and inter-bank credits, and the liquidity requirements of our clients;
- the level and volatility of interest rates, the valuation of the U.S. dollar relative to other currencies in which we record revenue or

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accrue expenses and the performance and volatility of securities, credit, currency and other markets in the U.S. and internationally;

- the credit quality, credit-agency ratings and fair values of the securities in our investment securities portfolio, a deterioration or downgrade of which could lead to other-than-temporary impairment of the respective securities and the recognition of an impairment loss in our consolidated statement of income;
- our ability to attract deposits and other low-cost, short-term funding, our ability to manage levels of such deposits and the relative portion of our deposits that are determined to be operational under regulatory guidelines and our ability to deploy deposits in a profitable manner consistent with our liquidity requirements and risk profile;
- the manner and timing with which the Federal Reserve and other U.S. and foreign regulators implement changes to the regulatory framework applicable to our operations, including implementation of the Dodd-Frank Act, the Basel III final rule and European legislation (such as the Alternative Investment Fund Managers Directive, Undertakings for Collective Investment in Transferable Securities Directives and Markets in Financial Instruments Directive II); among other consequences, these regulatory changes impact the levels of regulatory capital we must maintain, acceptable levels of credit exposure to third parties, margin requirements applicable to derivatives, and restrictions on banking and financial activities. In addition, our regulatory posture and related expenses have been and will continue to be affected by changes in regulatory expectations for global systemically important financial institutions applicable to, among other things, risk management, liquidity and capital planning and compliance programs, and changes in governmental enforcement approaches to perceived failures to comply with regulatory or legal obligations;
- adverse changes in the regulatory ratios that we are required or will be required to meet, whether arising under the Dodd-Frank Act or the Basel III final rule, or due to changes in regulatory positions, practices or regulations in jurisdictions in which we engage in banking activities, including changes in internal or external data, formulae, models, assumptions or other advanced systems used in the

calculation of our capital ratios that cause changes in those ratios as they are measured from period to period;

- increasing requirements to obtain the prior approval of the Federal Reserve or our other U.S. and non-U.S. regulators for the use, allocation or distribution of our capital or other specific capital actions or programs, including acquisitions, dividends and stock purchases, without which our growth plans, distributions to shareholders, share repurchase programs or other capital initiatives may be restricted;
- changes in law or regulation, or the enforcement of law or regulation, that may adversely affect our business activities or those of our clients or our counterparties, and the products or services that we sell, including additional or increased taxes or assessments thereon, capital adequacy requirements, margin requirements and changes that expose us to risks related to the adequacy of our controls or compliance programs;
- financial market disruptions or economic recession, whether in the U.S., Europe, Asia or other regions;
- our ability to promote a strong culture of risk management, operating controls, compliance oversight and governance that meet our expectations and those of our clients and our regulators;
- the results of, and costs associated with, governmental or regulatory inquiries and investigations, litigation and similar claims, disputes, or proceedings;
- our ability to develop, finalize and execute our plan to accelerate the next phase of our program to create cost efficiencies through changes in our operational processes and to further digitize our processes and interfaces with our clients. The objectives of this plan are to enhance the value and delivery of our products and services to clients and to identify and implement significant reductions in our cost structure. Any failure in whole or in part to achieve these objectives may, among other things, limit the attractiveness of our products or services to clients. This could reduce our competitive position, diminish the cost-effectiveness of our systems and processes or provide an insufficient return on our associated investment;
- the potential for losses arising from our investments in sponsored investment funds;
- the possibility that our clients will incur substantial losses in investment pools for

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which we act as agent, and the possibility of significant reductions in the liquidity or valuation of assets underlying those pools;

- our ability to anticipate and manage the level and timing of redemptions and withdrawals from our collateral pools and other collective investment products;
- the credit agency ratings of our debt and depository obligations and investor and client perceptions of our financial strength;
- adverse publicity, whether specific to State Street or regarding other industry participants or industry-wide factors, or other reputational harm;
- our ability to control operational risks, data security breach risks and outsourcing risks, our ability to protect our intellectual property rights, the possibility of errors in the quantitative models we use to manage our business and the possibility that our controls will prove insufficient, fail or be circumvented;
- our ability to expand our use of technology to enhance the efficiency, accuracy and reliability of our operations and our dependencies on information technology and our ability to control related risks, including cyber-crime and other threats to our information technology infrastructure and systems and their effective operation both independently and with external systems, and complexities and costs of protecting the security of our systems and data;
- our ability to grow revenue, manage expenses, attract and retain highly skilled people and raise the capital necessary to achieve our business goals and comply with regulatory requirements and expectations;
- changes or potential changes to the competitive environment, including changes due to regulatory and technological changes, the effects of industry consolidation and perceptions of State Street as a suitable service provider or counterparty;
- changes or potential changes in the amount of compensation we receive from clients for our services, and the mix of services provided by us that clients choose;
- our ability to complete acquisitions, joint ventures and divestitures, including the ability to obtain regulatory approvals, the ability to arrange financing as required and the ability to satisfy closing conditions;
- the risks that our acquired businesses and joint ventures will not achieve their anticipated financial and operational benefits or will not be integrated successfully, or that

the integration will take longer than anticipated, that expected synergies will not be achieved or unexpected negative synergies or liabilities will be experienced, that client and deposit retention goals will not be met, that other regulatory or operational challenges will be experienced, and that disruptions from the transaction will harm our relationships with our clients, our employees or regulators;

- our ability to recognize emerging needs of our clients and to develop products that are responsive to such trends and profitable to us, the performance of and demand for the products and services we offer, and the potential for new products and services to impose additional costs on us and expose us to increased operational risk;
- changes in accounting standards and practices; and
- changes in tax legislation and in the interpretation of existing tax laws by U.S. and non-U.S. tax authorities that affect the amount of taxes due.

Actual outcomes and results may differ materially from what is expressed in our forward-looking statements and from our historical financial results due to the factors discussed in this section and elsewhere in this Form 10-Q or disclosed in our other SEC filings, including the risk factors discussed in our 2014 Form 10-K. Forward-looking statements in this Form 10-Q should not be relied on as representing our expectations or beliefs as of any date subsequent to the time this Form 10-Q is filed with the SEC. We undertake no obligation to revise our forward-looking statements after the time they are made. The factors discussed above are not intended to be a complete statement of all risks and uncertainties that may affect our businesses. We cannot anticipate all developments that may adversely affect our business or operations or our consolidated results of operations, financial condition or cash flows.
Forward-looking statements should not be viewed as predictions, and should not be the primary basis on which investors evaluate State Street. Any investor in State Street should consider all risks and uncertainties disclosed in our

SEC filings, including our filings under the Securities Exchange Act of 1934, in particular our annual reports on Form 10-K, our quarterly reports on Form 10-Q and our current reports on Form 8-K, or registration statements filed under the Securities Act of 1933, all of which are accessible on the SEC's website at www.sec.gov or on the “Investor Relations” section of our corporate website at www.statestreet.com.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

TABLE 1: OVERVIEW OF FINANCIAL RESULTS

	Quarters Ended September 30,		
(Dollars in millions, except per share amounts)	2015	2014	% Change
Total fee revenue	$2,108	$2,012	5 %
Net interest revenue	513	570	(10)
Gains (losses) related to investment securities, net	(2)	—	—
Total revenue	2,619	2,582	1
Provision for loan losses	5	2	
Total expenses	1,962	1,892	4
Income before income tax expense	652	688	(5)
Income tax expense	68	128	(47)
Net income from non-controlling interest	1	—	
Net income	$585	$560	4
Adjustments to net income:			
Dividends on preferred stock(1)	(42)	(18)	133
Net income available to common shareholders	$543	$542	—
Earnings per common share:			
Basic	$1.34	$1.28	5
Diluted	1.32	1.26	5
Average common shares outstanding (in thousands):			
Basic	406,612	421,974	
Diluted	412,167	429,736	
Cash dividends declared per common share	$.34	$.30	
Return on average common equity	11.3 %	10.6 %	

	Nine Months Ended September 30,		
(Dollars in millions, except per share amounts)	2015	2014	% Change
Total fee revenue	$6,250	$5,975	5 %
Net interest revenue	1,594	1,686	(5)
Gains (losses) related to investment securities, net	(6)	4	(250)
Total revenue	7,838	7,665	2
Provision for loan losses	11	6	83
Total expenses	6,193	5,770	7
Income before income tax expense	1,634	1,889	(13)
Income tax expense	219	344	(36)
Net income from non-controlling interest	1	—	
Net income	$1,416	$1,545	(8)
Adjustments to net income:			
Dividends on preferred stock(1)	(102)	(43)	137
Earnings allocated to participating securities(2)	(1)	(2)	(50)
Net income available to common shareholders	$1,313	$1,500	(12)
Earnings per common share:			
Basic	$3.20	$3.52	(9)
Diluted	3.16	3.45	(8)
Average common shares outstanding (in thousands):			
Basic	409,816	426,775	
Diluted	415,772	434,510	

Cash dividends declared per common share	$.98	$.86
Return on average common equity	9.2 %	10.0 %

(1) Refer to note 10 to the consolidated financial statements included in this Form 10-Q for additional information regarding our preferred stock dividends.
(2) Refer to note 16 to the consolidated financial statements included in this Form 10-Q.

The following “Highlights” and “Financial Results” sections provide information related to significant events, as well as highlights of our consolidated financial results for the third quarter of 2015 presented in Table 1: Overview of Financial Results. More detailed information about our consolidated financial results, including comparisons of our financial results for the third quarter of 2015 to those for the third quarter of 2014 and for the nine months ended September 30, 2015 to those for nine months ended September 30, 2014, is provided under “Consolidated Results of Operations,” which follows these sections. In this Management’s Discussion and Analysis, where we describe the effects of changes in foreign exchange rates, those effects are determined by applying applicable weighted average foreign exchange rates from the relevant 2014 period to the relevant 2015 results.

Highlights

- In October 2015, we announced a multi-year plan to accelerate the next phase of our program to create cost efficiencies through changes in our operational processes and to further digitize our processes and interfaces with our clients. The objectives of this plan are to enhance the value and delivery of our products and services to our clients and to identify and implement significant reductions in our cost structure. We are targeting approximately $500 million in annualized savings from this plan, when fully implemented over approximately the next four to five years.
- In the third quarter of 2015, we recorded a $59 million reduction of an Italian deferred tax liability as a consequence of our European legal entity restructuring activities.
- Asset servicing and asset management fees decreased 1% and 9%, respectively, in the third quarter of 2015 compared to the third quarter of 2014, primarily due the impact of the stronger U.S. dollar.
- In the third quarter of 2015, we secured new business of an estimated $141 billion in assets to be serviced; of that total, approximately $101 billion was installed prior to September 30, 2015, with the remaining balance expected to be installed in the remainder of 2015 or later.
- In the third quarter of 2015, we declared quarterly common stock dividends of $0.34 per share, totaling approximately $138 million which were paid in October 2015.

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MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

- Under a purchase program approved by our Board of Directors in March 2015 which authorizes us to purchase up to $1.8 billion of our common stock through June 30, 2016, we purchased approximately 4.8 million shares of our common stock at an average per-share cost of $72.43 and an aggregate cost of approximately $350 million during the third quarter of 2015.

Additional information with respect to our common stock purchase program and stock dividends is provided under "Financial Condition - Capital" in this Management's Discussion and Analysis.

Financial Results

- Total revenue in the third quarter of 2015 increased 1% compared to the third quarter of 2014, primarily due to a 5% increase in total fee revenue, partially offset by a decline in net interest revenue.
- Total revenue in the third quarter of 2015 includes an $83 million pre-tax gain related to the sale of commercial real estate acquired as a result of the Lehman Brothers bankruptcy. The increase in total revenue was largely offset by a decrease of $80 million related to the stronger U.S. dollar when compared to the third quarter of 2014.
- Total expenses in the third quarter of 2015 increased 4% compared to the third quarter of 2014, primarily driven by $75 million of pre-tax severance costs related to targeted staff reductions taken to better calibrate our expenses to the current environment, partially offset by a $9 million decrease in occupancy and a $67 million dollar decrease in other expenses.
- Total expenses in the third quarter of 2015 benefited from the stronger U.S. dollar by approximately $63 million compared to the third quarter of 2014.
- Return on average common shareholders' equity in the third quarter of 2015 increased to 11.3% from 10.6% in the third quarter of 2014.

CONSOLIDATED RESULTS OF OPERATIONS

This section discusses our consolidated results of operations for the third quarter and first nine months of 2015 compared to the same periods in 2014, and should be read in conjunction with the consolidated financial statements and accompanying condensed notes to the consolidated financial statements included in this Form 10-Q.

Total Revenue

TABLE 2: TOTAL REVENUE

	Quarters Ended September 30,		
(Dollars in millions)	2015	2014	% Change
Fee revenue:			
Servicing fees	$1,294	$1,302	(1)%
Management fees	287	316	(9)
Trading services:			
Foreign exchange trading	177	161	10
Brokerage and other trading services	117	117	—
Total trading services	294	278	6
Securities finance	113	99	14
Processing fees and other	120	17	606
Total fee revenue	2,108	2,012	5
Net interest revenue:			
Interest revenue	614	671	(8)
Interest expense	101	101	—
Net interest revenue	513	570	(10)
Gains (losses) related to investment securities, net	(2)	—	
Total revenue	$2,619	$2,582	1

(Dollars in millions)	Nine Months Ended September 30, 2015	2014	% Change
Fee revenue:			
Servicing fees	$3,892	$3,828	2 %
Management fees	892	908	(2)
Trading services:			
Foreign exchange trading	547	439	25
Brokerage and other trading services	352	352	—
Total trading services	899	791	14
Securities finance	369	331	11
Processing fees and other	198	117	69
Total fee revenue	6,250	5,975	5
Net interest revenue:			
Interest revenue	1,885	1,976	(5)
Interest expense	291	290	—
Net interest revenue	1,594	1,686	(5)
Gains (losses) related to investment securities, net	(6)	4	
Total revenue	$7,838	$7,665	2

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FEE REVENUE

Servicing and management fees collectively comprised approximately 75% and 77%, of our total fee revenue in the third quarter and first nine months of 2015, respectively, compared to approximately 80% and 79%, in the third quarter and first nine months of 2014, respectively. The level of these fees is influenced by several factors, including the mix and volume of our assets under custody and administration and our assets under management, the value and type of securities positions held (with respect to assets under custody) and the volume of portfolio transactions, and the types of products and services used by our clients, and is generally affected by changes in worldwide equity and fixed-income security valuations and trends in market asset class preferences.

Generally, servicing fees are affected by changes in daily average valuations of assets under custody and administration. Additional factors, such as the relative mix of assets serviced, the level of transaction volumes, changes in service level, the nature of services provided, balance credits, client minimum balances, pricing concessions, the geographical location in which services are provided and other factors, may have a significant effect on our servicing fee revenue.

Generally, management fees are affected by changes in month-end valuations of assets under management. Management fees for certain components of managed assets, such as ETFs, are affected by daily average valuations of assets under management. Management fee revenue is more sensitive to market valuations than servicing fee revenue, as a higher proportion of the underlying services provided, and the associated management fees earned, are dependent on equity and fixed-income security valuations. Additional factors, such as the relative mix of assets managed, may have a significant effect on our management fee revenue. While certain management fees are directly determined by the values of assets under management and the investment strategies employed, management fees may reflect other factors as well, including performance fee

arrangements, discussed later in this section, as well as our relationship pricing for clients using multiple services. Asset-based management fees for actively managed products are generally charged at a higher percentage of assets under management than for passive products. Actively managed products may also include performance fee arrangements which are recorded when the performance period is complete. Performance fees are generated when the performance of certain managed portfolios exceeds benchmarks specified in the management agreements. Generally, we experience more volatility with performance fees than with more traditional management fees.

In light of the above, we estimate, using relevant information as of September 30, 2015 and assuming that all other factors remain constant, that: (1) a 10% increase or decrease in worldwide equity valuations, over the relevant periods for which our servicing and management fees are calculated, would result in a corresponding change in our total revenue of approximately 2%; and (2) a 10% increase or decrease in worldwide fixed income security valuations, over the relevant periods for or on which our servicing and management fees are calculated, would result in a corresponding change in our total revenue of approximately 1%.

See Table 3: Daily, Month-end and Year-end Indices for selected equity market indices. While the specific indices presented are indicative of general market trends, the asset types and classes relevant to individual client portfolios can and do differ, and the performance of associated relevant indices can therefore differ from the performance of the indices presented.

Daily averages and the averages of month-end indices demonstrate worldwide changes in equity markets that affect our servicing and management fee revenue. Quarter-end indices affect the values of assets under custody and administration and assets under management as of those dates. The index names listed in the table are service marks of their respective owners.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

TABLE 3: DAILY, MONTH-END AND YEAR-END INDICES

	Daily Averages of Indices Quarters Ended September 30,			Averages of Month-End Indices Quarters Ended September 30,			Quarter-End Indices As of September 30,		
	2015	2014	% Change	2015	2014	% Change	2015	2014	% Change
S&P 500®	2,027	1,976	3 %	1,999	1,969	2 %	1,920	1,972	(3)%
NASDAQ®	4,924	4,483	10	4,842	4,481	8	4,620	4,493	3
MSCI EAFE®	1,785	1,924	(7)	1,754	1,901	(8)	1,644	1,846	(11)
MSCI Emerging	860	1,067	(19)	837	1,053	(21)	792	1,005	(21)

	Daily Averages of Indices Nine Months Ended September 30,			Averages of Month-End Indices Nine Months Ended September 30,		
	2015	2014	% Change	2015	2014	% Change
S&P 500®	2,064	1,905	8 %	2,047	1,910	7 %
NASDAQ®	4,928	4,298	15	4,891	4,313	13
MSCI EAFE®	1,836	1,920	(4)	1,827	1,918	(5)
MSCI Emerging	948	1,017	(7)	940	1,014	(7)

Table 2: Total Revenue provides the breakout of fee revenue for the third quarter and first nine months of 2015 and 2014.

Servicing Fees

Servicing fees in the third quarter of 2015 decreased 1% compared to the same period in 2014, primarily due to the impact of the stronger U.S. dollar of approximately $50 million and weaker international equity markets, partially offset by net new business and higher transaction volumes. In the nine months ended September 30, 2015, servicing fees increased 2% compared to the same period in 2014, primarily as a result of the positive revenue impact of net new business (revenue added from new servicing business installed less revenue lost from the removal of assets serviced) and stronger U.S. equity markets, offset by the impact of the stronger U.S. dollar and weaker international markets. In both the third quarter and first nine months of 2015, servicing fees generated outside the U.S. were approximately 41% of total servicing fees compared to 42% for both the third quarter and first nine months of 2014.

The decrease in total assets under custody and administration as of September 30, 2015 compared to both December 31, 2014 and September 30, 2014 primarily resulted from weaker global equity markets, partially offset by net new business. Asset levels as of September 30, 2015 did not reflect the estimated $141 billion of new business in assets to be serviced awarded to us in the third quarter of 2015 and prior periods but not installed prior to September 30, 2015. This new business will be reflected in assets under custody and administration in future periods after installation and will generate servicing fee revenue in subsequent periods.

With respect to these new assets, we will provide various services, including accounting, bank loan servicing, compliance reporting and monitoring, custody, depository banking services, foreign exchange, fund administration, hedge fund servicing, middle-office outsourcing, performance and analytics, private equity administration, real estate administration, securities finance, transfer agency, and wealth management services.

The value of assets under custody and administration is a broad measure of the relative size of various markets served. Changes in the values of assets under custody and administration from period to period do not necessarily result in proportional changes in our servicing fee revenue.

TABLE 4: COMPONENTS OF ASSETS UNDER CUSTODY AND ADMINISTRATION

(Dollars in billions)	September 30, 2015	December 31, 2014	September 30, 2014
Mutual funds	$6,698	$6,992	$7,035
Collective funds	6,883	6,949	6,919
Pension products	5,497	5,746	5,780
Insurance and other products	8,187	8,501	8,731

Total	$27,265	$28,188	$28,465

TABLE 5: COMPOSITION OF ASSETS UNDER CUSTODY AND ADMINISTRATION

(Dollars in billions)	September 30, 2015	December 31, 2014	September 30, 2014
Equities	$14,223	$15,876	$15,616
Fixed-income	9,470	8,739	9,298
Short-term and other investments	3,572	3,573	3,551
Total	$27,265	$28,188	$28,465

TABLE 6: GEOGRAPHIC MIX OF ASSETS UNDER CUSTODY AND ADMINISTRATION[(1)]

(Dollars in billions)	September 30, 2015	December 31, 2014	September 30, 2014
North America	$20,536	$21,217	$21,255
Europe/Middle East/Africa	5,452	5,633	5,869
Asia/Pacific	1,277	1,338	1,341
Total	$27,265	$28,188	$28,465

[(1)] Geographic mix is based on the location at which the assets are serviced.

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Management Fees
Management fees in the third quarter and first nine months of 2015 decreased 9% and 2%, respectively, compared to the third quarter and first nine months of 2014, primarily due to the effects of the stronger U.S. dollar.
The stronger U.S. dollar had the effect of reducing management fees by approximately $11 million in the third quarter of 2015 compared to the same period in 2014.
Management fees generated outside the U.S. were approximately 34% and 35%, respectively, of total management fees for the third quarter and first nine months of 2015, compared to 38% and 37%, respectively, for the same periods in 2014.

TABLE 7: ASSETS UNDER MANAGMENT BY ASSET CLASS AND INVESTMENT APPROACH

(Dollars in billions)	September 30, 2015	December 31, 2014	September 30, 2014
Equity:			
Active	$29	$39	$40
Passive	1,237	1,436	1,371
Total Equity	1,266	1,475	1,411
Fixed-Income:			
Active	16	17	16
Passive	300	302	322
Total Fixed-Income	316	319	338
Cash(1)	380	399	410
Multi-Asset-Class Solutions:			
Active	26	30	34
Passive	85	97	104
Total Multi-Asset-Class Solutions	111	127	138
Alternative Investments(2):			
Active	17	17	17
Passive	113	111	107
Total Alternative Investments	130	128	124
Total	$2,203	$2,448	$2,421

(1) Includes both floating- and constant-net-asset-value portfolios held in commingled structures or separate accounts.
(2) Includes real estate investment trusts, currency and commodities, including SPDR® Gold Fund, for which State Street is not the investment manager, but acts as distribution agent.

TABLE 8: EXCHANGE-TRADED FUNDS BY ASSET CLASS(1)

(Dollars in billions)	September 30, 2015	December 31, 2014	September 30, 2014
Alternative Investments(2)	$35	$38	$40
Cash	3	1	1
Equity	323	388	338
Fixed-income	39	39	37
Total Exchange-Traded Funds	$400	$466	$416

(1) ETFs are a component of assets under management presented in the preceding table.
(2) Includes SPDR® Gold Fund, for which State Street is not the investment manager, but acts as distribution agent.

TABLE 9: GEOGRAPHIC MIX OF ASSETS UNDER MANAGEMENT(1)

(Dollars in billions)	September 30, 2015	December 31, 2014	September 30, 2014
North America	$1,409	$1,568	$1,502

Europe/Middle East/Africa	500	559	565
Asia/Pacific	294	321	354
Total	$2,203	$2,448	$2,421

(1) Geographic mix is based on client location or fund management location.

In asset management, we experienced net outflows of approximately $133 billion between December 31, 2014 and September 30, 2015 primarily composed of approximately $82 billion of net outflows from long-term institutional portfolios, approximately $33 billion of net outflows from ETFs and approximately $18 billion of outflows from cash products. The decrease in total assets under management at September 30, 2015 compared to December 31, 2014 resulted primarily from outflows from SPY, our S&P 500 ETF, outflows from institutional equity products driven by client re-balancing and cash needs, weaker global equity market levels and the impact of the strengthening U.S. dollar. The decrease in total assets under management as of September 30, 2015 compared to September 30, 2014 resulted from net outflows and the strengthening U.S. dollar, partially offset by stronger U.S. equity markets.

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TABLE 10: ACTIVITY IN ASSETS UNDER MANAGEMENT BY PRODUCT CATEGORY

(In billions)	Equity	Fixed-Income	Cash[2]	Multi-Asset-Class Solutions	Alternative Investments[3]	Total
Balance as of September 30, 2014	$1,411	$ 338	$410	$ 138	$124	$2,421
Long-term institutional inflows[1]	85	20	—	7	4	116
Long-term institutional outflows[1]	(80)	(45)	—	(9)	(3)	(137)
Long-term institutional flows, net	5	(25)	—	(2)	1	(21)
ETF flows, net	37	2	1	—	(2)	38
Cash fund flows, net	—	—	(10)	—	—	(10)
Total flows, net	42	(23)	(9)	(2)	(1)	7
Market appreciation	39	14	—	(7)	9	55
Foreign exchange impact	(17)	(10)	(2)	(2)	(4)	(35)
Total market/foreign exchange impact	22	4	(2)	(9)	5	20
Balance as of December 31, 2014	1,475	319	399	127	128	2,448
Long-term institutional inflows[1]	218	48	—	42	30	338
Long-term institutional outflows[1]	(291)	(48)	—	(53)	(28)	(420)
Long-term institutional flows, net	(73)	—	—	(11)	2	(82)
ETF flows, net	(38)	3	2	—	—	(33)
Cash fund flows, net	—	—	(18)	—	—	(18)
Total flows, net	(111)	3	(16)	(11)	2	(133)
Market appreciation	(79)	—	—	(2)	9	(72)
Foreign exchange impact	(19)	(6)	(3)	(3)	(9)	(40)
Total market/foreign exchange impact	(98)	(6)	(3)	(5)	—	(112)
Balance as of September 30, 2015	$1,266	$ 316	$380	$ 111	$130	$2,203

[1] Amounts represent long-term portfolios, excluding ETFs.
[2] Includes both floating- and constant-net-asset-value portfolios held in commingled structures or separate accounts.
[3] Includes real estate investment trusts, currency and commodities, including SPDR® Gold Fund, for which State Street is not the investment manager, but acts as distribution agent.

The net outflows of approximately $133 billion in assets under management between September 30, 2015 and December 31, 2014 presented in the preceding table did not include approximately $22 billion of new asset management business, which was awarded to SSGA but not installed as of September 30, 2015. This new business will be reflected in assets under management in future periods after installation, and will generate management fee revenue in subsequent periods. Net outflows in the third quarter reflect significant outflows from a single client. This client is anticipated to continue its reallocations during the remainder of 2015 and into 2016. This reallocation will impact the AUM that we report in future periods.

Total assets under management as of September 30, 2015 included managed assets lost but not yet liquidated. Lost business occurs from time to time and it is difficult to predict the timing of client behavior in transitioning these assets. This timing can vary significantly.

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Trading Services
TABLE 11: TRADING SERVICES REVENUE

(Dollars in millions)	Quarters Ended September 30, 2015	2014	% Change
Foreign exchange trading:			
Direct sales and trading	$108	$101	7 %
Indirect foreign exchange trading	69	60	15
Total foreign exchange trading	177	161	10
Brokerage and other trading services:			
Electronic foreign exchange services	46	44	5
Other trading, transition management and brokerage	71	73	(3)
Total brokerage and other trading services	117	117	—
Total trading services revenue	$294	$278	6

(Dollars in millions)	Nine Months Ended September 30, 2015	2014	% Change
Foreign exchange trading:			
Direct sales and trading	$331	$251	32 %
Indirect foreign exchange trading	216	188	15
Total foreign exchange trading	547	439	25
Brokerage and other trading services:			
Electronic foreign exchange services	138	135	2
Other trading, transition management and brokerage	214	217	(1)
Total brokerage and other trading services	352	352	—
Total trading services revenue	$899	$791	14

Trading services revenue is composed of revenue generated by foreign exchange, or FX, trading, as well as revenue generated by brokerage and other trading services. We primarily earn FX trading revenue by acting as a principal market maker. We offer a range of FX products, services and execution models. Most of our FX products and execution services can be grouped into three broad categories, which are further explained below: "direct sales and trading," "indirect FX trading" and "electronic FX services." With respect to electronic FX services, we provide an execution venue, but do not act as agent or principal.

We also offer a range of brokerage and other trading products tailored specifically to meet the needs of the global pension community, including transition management and commission recapture. In addition, we act as distribution agent for the SPDR® Gold ETF. These products and services are generally differentiated by our role as an agent of the institutional investor. Revenue earned from these services is recorded in other trading, transition management and brokerage revenue within brokerage and other trading services revenue.

Our FX trading revenue is influenced by multiple factors, including: the volume and type of client FX transactions and related spreads; currency volatility, reflecting market conditions; and our management of exchange rate, interest rate and other market risks associated with our foreign exchange activities. The relative impact of these factors on our total FX trading revenues often differs from period to period. For example, assuming all other factors remain constant, increases or decreases in volumes or spreads across product mix tend to result in increases or decreases, as the case may be, in client-related FX revenue. Revenue earned from direct sales and trading and indirect FX trading is recorded in FX trading revenue.

Total FX trading revenue increased 10% and 25%, for the third quarter and first nine months of 2015, respectively, compared to the same periods in 2014, primarily the result of higher volatility, market making activities and client volumes.

We enter into FX transactions with clients and investment managers that contact our trading desk directly. These trades are all executed at negotiated rates. We refer to this activity, and our principal market-making activities, as “direct sales and trading” and it includes many transactions for funds serviced by third party custodians or prime brokers, as well as those funds under custody at State Street. Direct sales and trading revenue represented 61% of total foreign exchange trading revenue for both the three and nine month periods ended September 30, 2015, respectively, as compared to 63% and 57% in the same periods in 2014.

Alternatively, clients or their investment managers may elect to route FX transactions to our FX desk through our asset-servicing operation; we refer to this activity as “indirect FX trading,” and, in all cases, we are the funds custodian. We execute indirect FX trades as a principal at rates disclosed to our clients. Estimated indirect sales and trading revenue represented 39% of total foreign exchange trading revenue for both the three and nine month periods ended September 30, 2015, respectively, as compared to 37% and 43% in the same periods in 2014. We calculate revenue for indirect FX trading using an attribution methodology. This methodology takes into consideration estimated mark-ups/downs and observed client volumes. Direct sales and trading revenue is all other FX trading revenue other than the revenue attributed to indirect FX trading.

Our clients that utilize indirect FX trading can, in addition to executing their FX transactions through dealers not affiliated with us, transition from indirect FX trading to either direct sales and trading execution, including our “Street FX” service, or to one of our electronic trading platforms. Street FX, in which we continue to act as a principal market maker, enables our clients to define their FX execution strategy and automate the FX trade execution process, both for funds under custody with us as well as those under custody at another bank.

Our direct sales and trading revenue increased 7% and 32%, in the third quarter and first nine months of 2015, respectively, as compared to the same periods of 2014. The increases primarily resulted from higher currency volatility, market making activities and client volumes. Our estimated indirect FX trading revenue increased 15% in both the third quarter and first nine months of 2015, respectively, compared to the same periods of 2014. The increase mainly resulted from higher currency volatility, client volumes and spreads.

We continue to expect that some clients may choose, over time, to reduce their level of indirect FX trading transactions in favor of other execution methods, including either direct sales and trading transactions or electronic FX services which we provide. To the extent that clients shift to other execution methods that we provide, our FX trading revenue may decrease, even if volumes remain consistent.

Total brokerage and other trading services revenue was flat in the third quarter and first nine months of 2015, compared to the same periods of 2014. Our clients may choose to execute FX transactions through one of our electronic trading platforms. These transactions generate revenue through a "click" fee. Revenue from such electronic FX services increased 5% in the third quarter of 2015 and 2% for the first nine months of 2015 compared to the same periods of 2014.

The 3% and 1% decrease in other trading, transition management and brokerage revenue for the third quarter and first nine months of 2015, respectively, compared to the same periods of 2014 was primarily due to a decrease in transition management revenue, partially offset by an increase in other trading revenue. In recent years, our transition management revenue was adversely affected by compliance issues in our U.K. business during 2010 and 2011. The reputational and regulatory impact of those compliance issues may adversely affect our transition management revenue in future periods.

Securities Finance

Our securities finance business consists of three components: (1) an agency lending program for SSGA-managed investment funds with a broad range of investment objectives, which we refer to as the SSGA lending funds, (2) an agency lending program for third-party investment managers and asset owners, which we refer to as the agency lending funds and (3) security lending transactions which we

enter into as principal, which we refer to as our enhanced custody business.

See Table 2: Total Revenue for the comparison of securities finance revenue for the third quarter and first nine months of 2015 and 2014.

Securities finance revenue earned from our agency lending activities, which is composed of our split of both the spreads related to cash collateral and the fees related to non-cash collateral, is principally a function of the volume of securities on loan, the interest-rate spreads and fees earned on the underlying collateral, and our share of the fee split.

As principal, our enhanced custody business borrows securities from the lending client and then lends such securities to the subsequent borrower, either a State Street client or a broker/dealer. We act as principal when the lending client is unable to, or elects not to, transact directly with the market and requires us to execute the transaction and furnish the securities. In our role as principal, we provide support to the transaction through our credit rating. While we source a significant proportion of the securities furnished by us in our role as principal from third parties, we have the ability to source securities through our assets under custody and administration, from clients who have designated State Street as an eligible borrower.

Securities finance revenue increased 14% and 11%, in the third quarter and first nine months of 2015, respectively, compared to the same periods of 2014. The increase was primarily the result of new business from our enhanced custody business.

Market influences may continue to affect client demand for securities finance, and as a result our revenue from, and the profitability of, our securities lending activities in future periods. In addition, recently effective regulatory changes may affect the volume of our securities lending activity and related revenue and profitability in future periods.

Processing Fees and Other

Processing fees and other revenue includes diverse types of fees and revenue, including fees from our structured products business, fees from software licensing and maintenance, equity income from our joint venture investments, gains and losses on sales of leased equipment and other assets, and amortization of our tax-advantaged investments. Processing fees and other revenue increased 606% and 69%, in the third quarter and first nine months of 2015, respectively, compared to the same periods of 2014, as shown in Table 2: Total Revenue. The increases were mainly due to the impact of an $83 million pre-tax gain related to the sale of

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commercial real estate acquired as a result of the Lehman Brothers bankruptcy.

NET INTEREST REVENUE

See Table 2: Total Revenue, for the breakout of interest revenue and interest expense for the quarters ended September 30, 2015 and 2014.

Net interest revenue is defined as interest revenue earned on interest-earning assets less interest expense incurred on interest-bearing liabilities. Interest-earning assets, which principally consist of investment securities, interest-bearing deposits with banks, repurchase agreements, loans and leases and other liquid assets, are financed

primarily by client deposits, short-term borrowings and long-term debt. Net interest margin represents the relationship between annualized fully taxable-equivalent net interest revenue and average total interest-earning assets for the period. It is calculated by dividing fully taxable-equivalent net interest revenue by average interest-earning assets. Revenue that is exempt from income taxes, mainly that earned from certain investment securities (state and political subdivisions), is adjusted to a fully taxable-equivalent basis using a federal statutory income tax rate of 35%, adjusted for applicable state income taxes, net of the related federal tax benefit.

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TABLE 12: AVERAGE BALANCES AND INTEREST RATES - FULLY TAXABLE-EQUIVALENT BASIS

	Quarters Ended September 30,							
	2015				2014			
(Dollars in millions; fully taxable-equivalent basis)	Average Balance	Interest Revenue/ Expense	Rate		Average Balance	Interest Revenue/ Expense	Rate	
Interest-bearing deposits with banks	$73,466	$53	.29	%	$63,160	$53	.33	%
Securities purchased under resale agreements	4,838	18	1.51		3,249	9	1.05	
Trading account assets	1,338	—	—		985	—	—	
Investment securities	100,175	505	2.02		117,618	586	1.99	
Loans and leases	17,606	79	1.77		16,002	64	1.59	
Other interest-earning assets	24,001	2	.03		17,003	2	.05	
Average total interest-earning assets	$221,424	$657	1.18		$218,017	$714	1.30	
Interest-bearing deposits:								
U.S.	$36,033	$15	.16	%	$24,144	$7	.11	%
Non-U.S.	101,297	13	.05		114,756	26	.09	
Securities sold under repurchase agreements	9,220	—	—		9,111	—	—	
Federal funds purchased	17	—	—		18	—	—	
Other short-term borrowings	3,791	1	.18		4,376	—	—	
Long-term debt	10,530	62	2.35		9,020	60	2.64	
Other interest-bearing liabilities	4,463	10	.88		7,386	8	.42	
Average total interest-bearing liabilities	$165,351	$101	.24		$168,811	$101	.24	
Interest-rate spread			.94	%			1.06	%
Net interest revenue—fully taxable-equivalent basis		$556				$613		
Net interest margin—fully taxable-equivalent basis			1.00	%			1.12	%
Tax-equivalent adjustment		(43)				(43)		
Net interest revenue—GAAP basis		$513				$570		

	Nine Months Ended September 30,							
	2015				2014			
(Dollars in millions; fully taxable-equivalent basis)	Average Balance	Interest Revenue/ Expense	Rate		Average Balance	Interest Revenue/ Expense	Rate	
Interest-bearing deposits with banks	$74,830	$161	.29	%	$50,153	$138	.37	%
Securities purchased under resale agreements	3,325	45	1.79		4,717	27	.78	
Trading account assets	1,234	—	—		947	1	.12	
Investment securities	107,216	1,574	1.96		117,681	1,752	1.98	
Loans and leases	17,711	229	1.73		15,227	183	1.61	
Other interest-earning assets	22,731	7	.04		15,138	5	.04	
Average total interest-earning assets	$227,047	$2,016	1.19		$203,863	$2,106	1.38	
Interest-bearing deposits:								
U.S.	$31,479	$34	.14	%	$19,016	$12	.09	%
Non-U.S.	105,347	33	.04		108,492	54	.07	
Securities sold under repurchase agreements	9,576	—	—		8,763	—	—	
Federal funds purchased	21	—	—		19	—	—	
Other short-term borrowings	4,211	5	.16		4,096	4	.12	

Long-term debt	9,809	185	2.51	9,340	186	2.66
Other interest-bearing liabilities	6,835	34	.65	7,237	34	.62
Average total interest-bearing liabilities	$167,278	$291	.23	$156,963	$290	.25
Interest-rate spread			0.96 %			1.13 %
Net interest revenue—fully taxable-equivalent basis		$1,725			$1,816	
Net interest margin—fully taxable-equivalent basis			1.02 %			1.19 %
Tax-equivalent adjustment		(131)			(130)	
Net interest revenue—GAAP basis		$1,594			$1,686	

Net interest revenue decreased 9% and 5%, on a fully taxable-equivalent basis in the third quarter and first nine months of 2015, respectively, compared to the same periods of 2014. The decrease was

generally the result of lower yields on interest-earning assets, as lower global interest rates affected our revenue from floating-rate assets, and the effects of the stronger U.S. dollar. The stronger U.S. dollar had the effect of reducing net interest revenue by approximately $14 million in the third quarter of 2015 compared to the same period in 2014, partially offset by the benefit of higher levels of interest-earning assets and lower rates on interest paid.

Changes in the components of interest-earning assets and interest-bearing liabilities are discussed in more detail below. Additional detail about the components of interest revenue and interest expense is provided in note 14 to the consolidated financial statements included in this Form 10-Q.

Average total interest-earning assets were higher for the third quarter and first nine months of 2015 compared to the same periods in 2014 as a result of elevated levels of client deposits invested in interest-bearing deposits with banks, higher average loans and leases and higher levels of cash collateral (included in other interest-earning assets in Table 12: Average Balances and Interest Rates - Fully Taxable-Equivalent Basis) provided in connection with our enhanced custody business.

The higher level of investment in interest-bearing deposits with banks resulted from higher levels of client deposits during the third quarter and first nine months of 2015 compared to the same periods in 2014, discussed further below, while the increase in average loans and leases resulted from growth in mutual fund lending and our continued investment in senior secured bank loans.

During the past year, our clients have continued to place elevated levels of deposits with us, as central bank actions have resulted in high levels of liquidity and low global interest rates. We evaluate deposits as either inherent in our relationship with our custodial clients, which we generally invest in our investment portfolio, or transient, or excess, deposits, which we generally deposit with central banks. Deposits with central banks generate low returns. Consequently, the elevated levels of these transient deposits have contributed to a reduction of our net interest margin relative to historical levels.

The deposits with central banks are also included in our total consolidated assets, and higher deposit levels impact our regulatory leverage ratios. We have been engaging in discussions with clients regarding deposit levels and during the third quarter of 2015 we took action to better balance our clients' cash management needs with our economic and regulatory objectives. These efforts resulted in a reduction in client deposits from June 30, 2015, mainly occurring toward the end of the third quarter of 2015. Client deposit levels at September 30, 2015 of $186 billion decreased $44 billion from $231 billion at June 30, 2015, and average third quarter 2015 client deposits of $137 billion decreased $2 billion from $139 billion at the second quarter of 2015. Were global interest rates to increase, we would expect to see further decreases in client deposits; however, in general, we continue to anticipate higher levels of client deposits, irrespective of the interest rate environment, during periods of market stress.

The effects of the recent stronger U.S. dollar relative to other currencies, particularly the Euro, also negatively impacted our net interest revenue as we maintain a portion of our investment portfolio in Euro denominated securities. If European Central Bank, or ECB, monetary policy continues to pressure European interest rates downward and the U.S. dollar remains strong or strengthens, the negative effects on our net interest revenue may continue or worsen.

Negative interest rates on assets generate negative interest income. Conversely, negative interest rates on liabilities generate negative interest expense. These amounts are included within interest income and interest expense.

We recorded aggregate discount accretion in interest revenue of $75 million in the first nine months of 2015 related to the assets we consolidated onto our balance sheet in 2009 from our asset-backed commercial paper conduits. Subsequent to the commercial paper conduit consolidation in 2009, we have recorded total discount accretion in interest revenue of $2.10 billion (including $75 million in the first nine months of 2015, $119 million for the twelve months ended December 31, 2014, $137 million for the twelve months ended December 31, 2013, $215 million for the twelve months ended December 31, 2012, $220 million for the twelve months ended December 31, 2011, $712 million for the twelve months ended December 31, 2010 and $621 million for the twelve months ended December 31, 2009). The timing and ultimate recognition of any applicable discount accretion depends, in part, on factors that are outside of our control, including anticipated prepayment speeds and credit quality. The impact of these factors is uncertain and can be significantly influenced by general economic and financial market conditions. The timing and recognition of any applicable discount accretion can also be influenced by our ongoing management of the risks and other characteristics associated with our investment securities portfolio, including sales of securities which would otherwise generate interest revenue through accretion.

Depending on the factors discussed above, among others, we anticipate that until the former conduit securities remaining in our investment portfolio mature or are sold, discount accretion will continue to contribute to our net interest revenue, though generally in declining amounts. Assuming that we hold the remaining former conduit securities to maturity, all else being equal, we expect the remaining former conduit securities carried in our investment portfolio as of September 30, 2015 to generate discount accretion in future periods of approximately $233 million over their remaining terms, with approximately half of this discount accretion to be recorded over the next four years.

Interest-bearing deposits with banks averaged $73.47 billion and $74.83 billion, for the third quarter and first nine months of 2015, respectively, compared to $63.16 billion and $50.15 billion, respectively, for the same periods of 2014. These deposits reflected our maintenance of cash balances at the Federal Reserve, the ECB and other non-U.S. central banks both to satisfy regulatory reserve requirements, and due to the continued elevated levels of client deposits and our investment of the excess deposits with central banks.

While the actions taken in the third quarter of 2015 have reduced levels of client deposits, we expect to continue to invest deposits we deem as elevated in investment securities or short-term assets, including central bank deposits, depending on our assessment of the underlying characteristics of the deposits.

Average investment securities decreased to $100.18 billion, and $107.22 billion, for the third quarter and first nine months of 2015, respectively, compared to $117.62 billion and $117.68 billion, for the same periods of 2014, as we continue to optimize our balance sheet in light of the evolving regulatory environment. Detail with respect to our investment securities portfolio as of September 30, 2015 and December 31, 2014 is provided in note 3 to the consolidated financial statements included in this Form 10-Q.

Average loans and leases increased to $17.61 billion and $17.71 billion, for the third quarter and first nine months of 2015, respectively, compared to $16.00 billion and $15.23 billion, for the same periods of 2014. The increase was mainly related to mutual fund lending and our continued investment in senior secured bank loans. Mutual fund lending and senior secured bank loans averaged approximately $12.63 billion and $12.73 billion, respectively, for the third quarter and first nine months of 2015, compared to $10.62 billion and $9.96 billion, for the same periods of 2014.

Average loans and leases also include short-duration advances.

TABLE 13: U.S. AND NON-U.S. SHORT-DURATION ADVANCES

	Quarters Ended September 30,	
(In millions)	2015	2014
Average U.S. short-duration advances	$2,226	$2,372
Average non-U.S. short-duration advances	1,325	1,468
Average total short-duration advances	$3,551	$3,840
Average short-duration advances to average loans and leases	20 %	24 %

	Nine Months Ended September 30,	
(In millions)	2015	2014
Average U.S. short-duration advances	$2,284	$2,264
Average non-U.S. short-duration advances	1,432	1,463
Average total short-duration advances	$3,716	$3,727
Average short-duration advances to average loans and leases	21 %	24 %

The decline in the proportion of the average daily short-duration advances to average loans and leases is primarily due to growth in the other segments of the loan and lease portfolio. Short-duration advances provide liquidity to clients in support of their investment activities.

Although average short-duration advances decreased for the third quarter of 2015 and remained relatively flat for the first nine months of 2015 compared to the third quarter and first nine months of 2014, respectively, such average short-duration advances provided by us remained low relative to historical levels, primarily the result of higher levels of liquidity, including excess deposits, held by our clients.

Average other interest-earning assets increased to $24.00 billion and $22.73 billion, for the third quarter and first nine months of 2015, respectively, from $17.00 billion and $15.14 billion, for the third quarter and first nine months of 2014, respectively. Our average other interest-earning assets, largely associated with our enhanced custody business, comprised approximately 11% of our average total interest-earning assets for both the third quarter and first nine months of 2015, compared to approximately 7% of our average total interest-earning assets for both the third quarter and first nine months of 2014, as this business continued to grow. While the enhanced custody business, our principal securities lending service for custody clients. supports our overall profitability by generating securities finance revenue, it puts downward pressure on our net interest margin, as interest income on the receivable associated with the cash collateral we provide is earned at a lower rate compared to our investment securities portfolio.

Aggregate average interest-bearing deposits decreased to $137.33 billion from $138.90 billion for the third quarter and increased to $136.83 billion from $127.51 billion in the first nine months of 2015, as compared to the same periods of 2014. The higher levels for the first nine months of 2015 were primarily the result of increases in both U.S. and non-U.S. transaction accounts and time deposits. Future transaction account levels will be influenced by the underlying asset servicing business, client deposit behavior in reaction to management actions taken in the third quarter to reduce deposits, as well as market conditions, including the general levels of U.S. and non-U.S. interest rates.

Average other short-term borrowings decreased to $3.79 billion from $4.38 billion for the third quarter and increased to $4.21 billion from $4.10 billion in the first nine months of 2015 as compared to the same periods of 2014. The increase for the first nine months of 2015 was the result of a higher level of client demand for our commercial paper. The third quarter decline is a result of State Street's plans to phase-out its commercial paper program by July 1, 2016, consistent with the objectives of its 2015 recovery and resolution plan developed pursuant to the requirements of the Dodd-Frank Act. In the third quarter of 2014 we had no interest expense on short-term borrowings as compared to the third quarter of 2015, when interest rates paid increased to 0.2%. Interest rates paid in the first nine months of 2015 increased to 0.2% from 0.1% for the same period in 2014. The increase over both periods resulted from a reclassification of certain derivative contracts in 2014 that hedge our interest-rate risk on certain assets and liabilities.

Average long-term debt increased to $10.53 billion and $9.81 billion, for the third quarter and first nine months of 2015, respectively, from $9.02 billion and $9.34 billion, respectively, for the same periods of 2014. The increase primarily reflected the issuance of $1.0 billion of senior debt issued in December 2014 and $3.0 billion of senior debt issued in August 2015 which was offset by a $900 million extendible note called at the end of February 2015, the maturities of $500 million of senior debt in May 2014 and $250 million of senior debt in March 2014.

Average other interest-bearing liabilities decreased to $4.46 billion and $6.84 billion, for the third quarter and first nine months of 2015, respectively, from $7.39 billion and $7.24 billion, respectively, for the same periods of 2014, primarily the result of higher levels of cash collateral received from clients in connection with our enhanced custody business.

Several factors could affect future levels of our net interest revenue and margin, including the mix of client liabilities; actions of various central banks; changes in U.S. and non-U.S. interest rates; changes in the various yield curves around the world; the effectiveness of our efforts to reduce excess client deposits; revised or proposed regulatory capital or liquidity standards, or interpretations of those standards; the amount of discount accretion generated by the former conduit securities that remain in our investment securities portfolio; the yields earned on securities purchased compared to the yields earned on securities sold or matured; and changes in our enhanced custody business.

Based on market conditions and other factors, we continue to reinvest the majority of the proceeds from pay-downs and maturities of investment securities in highly-rated securities, such as U.S. Treasury and agency securities, municipal securities, federal agency mortgage-backed securities and U.S. and non-U.S. mortgage- and asset-backed securities. The pace at which we continue to reinvest and the types of investment securities purchased will depend on the impact of market conditions and other factors over time. We expect these factors and the levels of global interest rates to influence what effect our reinvestment program will have on future levels of our net interest revenue and net interest margin.

Gains (Losses) Related to Investment Securities, Net

We regularly review our investment securities portfolio to identify other-than-temporary impairment of individual securities. Additional information about investment securities, the gross gains and losses that compose the net gains from sales of securities and other-than-temporary impairment is provided in note 3 to the consolidated financial statements included in this Form 10-Q.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS (Continued)

TABLE 14: INVESTMENT SECURITIES GAINS (LOSSES), NET

	Quarters Ended September 30,		Nine Months Ended September 30,	
(In millions)	2015	2014	2015	2014
Net realized gains (losses) from sales of available-for-sale securities	$(2)	$—	$(5)	$15
Net impairment losses:				
Gross losses from other-than-temporary impairment	—	—	(1)	(1)
Losses reclassified (from) to other comprehensive income	—	—	—	(10)
Net impairment losses[1]	—	—	(1)	(11)
Gains (losses) related to investment securities, net	$(2)	$—	$(6)	$4
[1] Net impairment losses, recognized in our consolidated statement of income, were composed of the following:				
Impairment associated with expected credit losses	$—	$—	$—	$(10)
Impairment associated with management's intent to sell impaired securities prior to recovery in value	—	—	—	—
Impairment associated with adverse changes in timing of expected future cash flows	—	—	(1)	(1)
Net impairment losses	$—	$—	$(1)	$(11)

From time to time, in connection with our ongoing management of our investment securities portfolio, we sell available-for-sale securities to manage risk, to take advantage of favorable market conditions, to optimize our balance sheet for regulatory changes, or for other reasons. In the first nine months of 2015, we sold approximately $12.42 billion of such investment securities, compared to approximately $8.20 billion in the first nine months of 2014. We recorded $5 million of net realized losses and $15 million of net realized gains in the first nine months of 2015 and 2014, respectively, as presented in the preceding table.

PROVISION FOR LOAN LOSSES

We recorded a provision for loan losses of $5 million and $11 million in the third quarter and first nine months of 2015, respectively, compared to $2 million and $6 million, in the same periods in 2014. The provisions in both periods of 2014 and 2015 were recorded as a result of our exposure to certain senior secured bank loans to non-investment grade borrowers, which we purchased in connection with our participation in loan syndications in the non-investment-grade lending market. Increases in the provisions in the year-to-date comparison reflected growth of our senior secured loan portfolio. Additional information about these senior secured bank loans is provided under "Financial Condition - Loans and Leases" in this Management's Discussion and Analysis and in note 4 to the consolidated financial statements included in this Form 10-Q.

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EXPENSES
TABLE 15: EXPENSES

	Quarters Ended September 30,		
(Dollars in millions)	2015	2014	% Change
Compensation and employee benefits	$1,051	$953	10 %
Information systems and communications	265	242	10
Transaction processing services	201	199	1
Occupancy	110	119	(8)
Acquisition costs	7	12	(42)
Restructuring charges, net	3	8	(63)
Other:			
Professional services	136	97	40
Amortization of other intangible assets	48	54	(11)
Securities processing costs	40	8	400
Regulatory fees and assessments	31	17	82
Other	70	183	(62)
Total other	325	359	(9)
Total expenses	$1,962	$1,892	4
Number of employees at quarter-end	31,860	29,510	

	Nine Months Ended September 30,		
(Dollars in millions)	2015	2014	% Change
Compensation and employee benefits	$3,122	$3,088	1 %
Information systems and communications	761	730	4
Transaction processing services	599	583	3
Occupancy	332	348	(5)
Acquisition costs	15	48	(69)
Restructuring charges, net	4	33	(88)
Other:			
Professional services	368	318	16
Amortization of other intangible assets	147	162	(9)
Securities processing costs	75	39	92
Regulatory fees and assessments	90	55	64
Other	680	366	86
Total other	1,360	940	45
Total expenses	$6,193	$5,770	7

Total expenses increased 4% and 7% in the third quarter and first nine months of 2015, respectively, compared to the same periods in 2014. Total expenses in the third quarter of 2015 and first nine months of 2015 benefited from the stronger U.S. dollar by approximately $63 million and $200 million respectively, compared to same periods in 2014.
Compensation and employee benefits expenses increased by 10% and 1% in the third quarter and first nine months of 2015, respectively, compared to the same periods in 2014. These increases were primarily driven by $75 million of pre-tax severance costs in the third quarter of 2015 related to targeted staff reductions.
Other expenses decreased 9% and increased 45% in the third quarter and first nine months of 2015,

respectively, compared to the same periods in 2014. The increase in the first nine months of 2015 was primarily due to a first quarter 2015 legal accrual of $150 million and a second quarter 2015 legal accrual of $250 million, each in connection with our indirect foreign exchange business. In addition, higher levels of regulatory fees and assessments also contributed to the increases. The decrease in the third quarter of 2015 was primarily due to a third-quarter 2015 gain of $41 million related to a recovery from certain Lehman Brothers claims, as compared to the same period in 2014. The legal accrual is further discussed under "Legal and Regulatory Matters" in note 8 to the consolidated financial statements included in this Form 10-Q.

Our compliance obligations have increased significantly due to new regulations in the U.S. and internationally that have been adopted or proposed in response to the financial crisis. As a systemically important financial institution, we are subject to enhanced supervision and prudential standards. Our status as a global systemically important bank, or G-SIB, has also resulted in heightened prudential and conduct expectations of our U.S. and international regulators with respect to our capital and liquidity management and our compliance and risk oversight programs. These heightened expectations have increased our regulatory compliance costs, including personnel and systems, as well as significant additional implementation and related costs to enhance our regulatory compliance programs. We anticipate that these evolving and increasing regulatory compliance requirements and expectations will continue to affect our expenses. Our employee compensation and benefits, information systems and other expenses could increase, as we further adjust our operations in response to new or proposed requirements and heightened expectations.

Acquisition Costs

In the third quarter and first nine months of 2015, we recorded acquisition costs of $7 million and $15 million, respectively, compared to $12 million and$48 million, in the same periods in 2014. These amounts related to previously disclosed acquisitions.

Restructuring Charges

In the third quarter of 2015, we recorded $3 million net restructuring charges compared to $8 million in the same period of 2014. In the first nine months of 2015, we recorded net restructuring charges of $4 million compared to $33 million in the same period in 2014. The amounts recorded in the third quarter of 2015 mainly related to our recently completed Business Operations and Information Technology Transformation program.

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Income Tax Expense

Income tax expense was $68 million in the third quarter of 2015 compared to $128 million in the third quarter of 2014. In the first nine months of 2015 and 2014, income tax expense was $219 million and $344 million, respectively. The decrease in tax expense was primarily due to the effects of legal accruals of $400 million recorded in 2015. Our effective tax rate for the first nine months of 2015 was 13.4% compared to 18.2% in the same period of 2014. The first nine months of 2015 included effects of the approval of a tax refund for prior years and the reduction of $59 million for an Italian deferred tax liability, partially offset by a change in New York tax law.

LINE OF BUSINESS INFORMATION

We have two lines of business: Investment Servicing and Investment Management. The results of operations for these lines of business are not necessarily comparable with those of other companies, including companies in the financial services industry. Information about our two lines of business, as well as the revenues, expenses and capital allocation methodologies associated with them, is provided in note 24 to the consolidated financial statements included in our 2014 Form 10-K.

The "Other" information presented below represents costs incurred that are not allocated to our business lines, including certain severance and restructuring costs, acquisition costs and certain provisions for legal contingencies.

"Other" for the third quarter and first nine months of 2015 included net costs of $85 million and $93 million, respectively, composed of the following -

- Net acquisition and restructuring costs of $10 million and $19 million, respectively; and
- Net severance costs of $75 million and $74 million, respectively.

"Other" for the third quarter and first nine months of 2014 included costs of $14 million and $157 million, respectively, composed of the following -

- Severance costs credits of $2 million associated with prior accruals for staff reductions and net severance costs of $74 million associated with staff reductions, respectively;
- Net acquisition and restructuring costs of $20 million and $81 million, respectively; and
- Credits to provisions for litigation exposure and other cost of $4 million in the third quarter of 2014.
- Provisions for legal contingencies of $2 million in the first nine months of 2014.

Prior reported results reflect reclassifications, for comparative purposes, related to management changes in methodologies associated with allocations of revenue and expenses reflected in line-of-business results for 2015.

Investment Servicing

TABLE 16: INVESTMENT SERVICING LINE OF BUSINESS RESULTS

	Three Months Ended September 30,			Nine Months Ended September 30,		
(Dollars in millions, except where otherwise noted)	2015	2014	% Change	2015	2014	% Change
Servicing fees	$1,294	$				