

**DISCOVER FINANCIAL SERVICES**

**Basel III Regulatory Capital Disclosures**

**For the Quarterly Period Ended June 30, 2024**

# DISCOVER FINANCIAL SERVICES

Basel III Regulatory Capital Disclosures for the Quarterly Period Ended June 30, 2024

## TABLE OF CONTENTS

Disclosure Road Map .....	1
Overview .....	2
Scope of Application .....	3
Capital Structure .....	5
Capital Adequacy .....	6
Capital Conservation Buffer and Stress Capital Buffer .....	7
Credit Risk: General Disclosures .....	8
Counterparty Credit Risk-Related Exposures: General Disclosures .....	10
Credit Risk Mitigation .....	11
Securitization .....	12
Equities Not Subject to Market Risk Rule .....	12
Interest Rate Risk for Non-Trading Activities .....	13

---

Except as otherwise indicated or unless the context otherwise requires, "Discover Financial Services," "Discover," "DFS," "we," "us," "our," and "the Company" refers to Discover Financial Services and its subsidiaries.

## Disclosure Road Map

The following table provides page references for disclosures within the Company's Quarter Report on Form 10-Q and Annual Report on Form 10-K relating to topics addressed in this Basel III disclosure report:

Topic	Subtopic	Basel III Report	2nd Quarter 2024 Form 10-Q	2023 Annual Report
		Page Reference(s)		
Overview	Introduction .....	2		
	Pending Sale of the Private Student Loan Portfolio .....	2	8	
	Pending Merger with Capital One Financial Corporation ..	2	8-9	1
	Basel III and Regulatory Capital Disclosure Report .....	2-3	26-27	125-126
	Basel III Finalization and Other Developments .....	3		54
Scope of Application	Basis of Consolidation .....	3		90-91
	Capital in Subsidiaries .....	3		
	Restrictions on Capital .....	3-4		22-23
Capital Structure	Regulatory Capital Instruments .....	5	23	120-121
	Regulatory Capital Ratios .....	6	26-27	125-126
Capital Adequacy	Capital Planning and Management .....	6	26-27	125-126
	Standardized Approach Risk-Weighted Assets .....	7		
	Risk-Based Capital Ratios .....	7	27	125-126
Capital Conservation Buffer and Stress Capital Buffer		7-8	66-67	73-76
Credit Risk: General Disclosures	Credit Risk Management Objectives and Policies .....	8		5-6, 11-20
	Delinquent Loans .....	8	13	93, 96-98, 101-112
	Allowance for Credit Losses .....	8	14-15	93-94
	Credit Risk Exposures .....	9-10	12-19	101-112
Counterparty Credit Risk-Related Exposures: General Disclosures	Counterparty Credit Risk Exposures .....	10-11	37-40	135-138
	Methodology Used to Assign Derivative Credit Limits .....	11		
	Policies for Securing, Valuing and Managing Collateral for Derivatives and Establishing Credit Reserves .....	11		
	Primary Types of Collateral for Derivatives Exposures .....	11		
Credit Risk Mitigation		11		
Securitization	Securitization Activities .....	12	19-21	112-113
Equities Not Subject to Market Risk Rule	Overview .....	12		
	Risk Weighting .....	12-13		
Interest Rate Risk for Non-Trading Activities		13	70-71	79-80

## Overview

### Introduction

Discover Financial Services ("DFS" or the "Company") is a digital banking and payment services company. The Company was incorporated in Delaware in 1960. The Company is a bank holding company ("BHC") under the Bank Holding Company Act of 1956 and a financial holding company under the Gramm-Leach-Bliley Act and therefore, the Company is subject to oversight, regulation and examination by the Board of Governors of the Federal Reserve System (the "FRB" or "Federal Reserve"). The Company provides digital banking products and services and payment services through its subsidiaries. The Company offers credit card loans, personal loans, home loans and deposit products to its customers. The Company also operates the Discover Network, the PULSE network ("PULSE") and Diners Club International ("Diners Club"), collectively known as the Discover Global Network. The Discover Network processes transactions for Discover-branded credit and debit 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 automated teller machines ("ATMs") domestically and internationally, as well as merchant acceptance throughout the United States of America ("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 credit and charge cards and/or provide card acceptance services.

The Company's banking subsidiary, Discover Bank, offers credit card loans, personal loans and home loans. Discover Bank also offers 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. Discover Bank 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.

### Pending Sale of The Private Student Loan Portfolio

In November 2023, the Company announced its Board of Directors had authorized management to explore the sale of its private student loan portfolio. The Company stopped accepting new applications for private student loans February 1, 2024, and as of June 30, 2024, the Company's private student loan portfolio was classified as loans held-for-sale. On July 17, 2024, Discover Bank entered into a purchase agreement to sell its private student loan portfolio and transfer servicing of the portfolio to a third-party servicer upon the sale. As of June 30, 2024, the principal balance of the private student loan portfolio was approximately \$10.1 billion. The purchase price payable to Discover Bank in the transaction is at a premium to the principal balance of the private student loan portfolio and, based on certain assumptions, is expected to be up to approximately \$10.8 billion. The transaction is expected to be completed in multiple closings by the end of 2024, subject to the satisfaction or waiver of customary closing conditions. For more information, see Discover's Current Report on Form 8-K filed with the Securities and Exchange Commission (the "SEC") on July 17, 2024.

### Pending Merger with Capital One Financial Corporation

On February 19, 2024, Discover and Capital One Financial Corporation ("Capital One") jointly announced that they entered into an agreement and plan of merger (the "Merger Agreement"), under which the companies will combine in an all-stock merger, which values Discover at \$35.3 billion based on the price of Capital One common stock on the last trading day before the public announcement of the merger. Under the terms of the Merger Agreement, holders of Discover common stock will receive 1.0192 shares of Capital One common stock for each share of Discover common stock they own. Capital One shareholders will own approximately 60% of the combined company and Discover shareholders will own approximately 40% of the combined company. The Merger Agreement contains customary representations and warranties, covenants and closing conditions. The Board of Directors of the combined company will have fifteen directors, consisting of twelve Capital One Board members and three Discover Board members to be named at a later date. For more information, see Discover's Current Report on Form 8-K filed with the SEC on February 22, 2024.

Completion of the proposed merger remains subject to approval by the FRB and the Office of the Comptroller of the Currency ("OCC") and other customary closing conditions, including the approval of both companies' shareholders.

### Basel III and Regulatory Capital Disclosure Report

DFS and Discover Bank are subject to regulatory capital rules issued by the Federal Reserve and FDIC, respectively, under the Basel Committee's December 2010 framework ("Basel III rules"). Under the Basel III rules, DFS and Discover Bank are classified as "standardized approach" entities.

The Basel III rules establish a more risk-sensitive approach to capital management and require the Company to publicly disclose certain qualitative and quantitative information regarding its capital structure and adequacy, credit risk and related mitigation policies, securitizations, equity exposures, operational risk and other matters. The qualitative and quantitative information included are commonly referred to as the "Pillar 3 Disclosures." The U.S. regulators have required the Pillar 3 Disclosures with an expressed objective of improving market discipline and encouraging sound risk management practices. This report provides the required disclosures or references to other publicly-available documents where they are located and includes information on the methodologies used to calculate risk-weighted assets ("RWAs"). See Note 11: Capital Adequacy in the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2024 ("2Q24 Form 10-Q") for a detailed discussion of the Basel III requirements.

This report should be read in conjunction with the Company's 2023 Form 10-K, 2Q24 Form 10-Q, Federal Reserve report form FR Y-9C for the year-to-date period ended June 30, 2024, and Discover Bank's Call Report ("Call Report") for the year-to-date period ended June 30, 2024, which include essential information on risk management policies and practices and regulatory capital ratios. In addition, this document contains a disclosure road map.

### **Basel III Finalization and Other Developments**

In July 2023, the Federal Reserve, the OCC and the FDIC issued a proposal to amend the risk-based capital framework, which includes replacing the current "advanced approach" with a new expanded risk-based approach. In addition, the proposal introduces new standardized approaches for credit risk, operational risk and credit valuation adjustment risk, and would significantly revise risk-based capital requirements for all banking institutions with assets of \$100 billion or more, including DFS. If adopted, the new requirements would be effective July 1, 2025, with a three-year transition period.

In August 2023, the Federal Reserve, the FDIC and the OCC (the "Agencies") issued a proposal that would require banking institutions in Categories II through IV of the tailoring framework, including DFS, and their insured depository institution subsidiaries with \$100 billion or more in assets such as Discover Bank, to have minimum levels of outstanding long-term debt. Under the proposed rule, a covered banking institution would be required to have a minimum outstanding amount of eligible long-term debt that is at least 6% of the institution's total risk-weighted assets, 2.5% of its total leverage exposure (if it is required to maintain a minimum supplementary leverage ratio) and 3.5% of its average total consolidated assets, whichever is greater. If adopted, banking institutions would have three years to comply with the new requirements, though the Agencies would retain the authority to accelerate or extend the transition period.

While we cannot currently predict the timing or substance of the finalization of these proposals or other regulatory changes, if any such change were adopted, it would likely revise the regulatory tailoring currently applicable to DFS and otherwise tighten the prudential regulatory requirements that would apply to DFS and increase our expenses.

### **Scope of Application**

#### **Basis of Consolidation**

The basis of consolidation used for regulatory reporting is the same as that used under accounting principles generally accepted in the U.S. ("GAAP"). See Note 1: Background and Basis of Presentation in the 2023 Form 10-K for details on the Company's principles of consolidation.

#### **Capital in Subsidiaries**

Discover Bank is the Company's only depository institution subsidiary. At June 30, 2024, the Company did not have any subsidiaries whose regulatory capital was less than the minimum required regulatory capital amount. The Company does not have any insurance subsidiaries subject to the Basel III rules.

#### **Restrictions on Capital**

The Federal Reserve requires a BHC to inform and consult with the Federal Reserve before declaring and paying any dividends that would cause an institution to become inadequately capitalized. The declaration and payment of future dividends are subject to the discretion of the Company's board of directors and compliance with the Stress Capital Buffer ("SCB") final rule. Banking laws and regulations and DFS' banking regulators may limit or prohibit the payment of dividends on, or DFS' repurchase of, DFS' stock at any time. As a result, there can be no assurance that DFS will declare and pay any dividends on or repurchase DFS stock in the future. At June 30, 2024, DFS was "well-capitalized" as defined in the Federal Reserve's Regulation Y.

The amount and size of any future dividends and share repurchases will depend on the Company's results of operations, financial condition, capital levels, cash requirements, future prospects, regulatory review and other factors. Under the Merger Agreement with Capital One, quarterly cash dividends on our common stock may not exceed \$0.70 per share without the prior written consent of Capital One and we have paused share repurchases through the completion of the merger. See Note 1: Background and Basis of Presentation in the 2Q24 Form 10-Q for additional information on the merger. Holders of the Company's shares of common stock are subject to the prior dividend rights of holders of the Company's preferred stock or the depositary shares representing such preferred stock outstanding. No dividend may be declared or paid or set aside for payment on the Company's common stock if full dividends have not been declared and paid on all outstanding shares of preferred stock in any dividend period. For more information, see "Business — Supervision and Regulation — Capital, Dividends and Share Repurchases" in the 2023 Form 10-K.

DFS, the 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. Banking laws and regulations and DFS' banking regulators may limit or prohibit the transfer of funds freely, either to or from the Company's subsidiaries, at any time. These laws, regulations and rules may hinder DFS' ability to access funds that it may need to make payments on its obligations or otherwise achieve its strategic objectives. For more information, see "Business — Supervision and Regulation — Capital, Dividends and Share Repurchases" in the 2023 Form 10-K.

The Federal Deposit Insurance Act ("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 June 30, 2024, Discover Bank met all applicable requirements to be deemed "well-capitalized."

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. For more information on FDIA regulations, see "Business — Supervision and Regulation — FDIA" in the 2023 Form 10-K.

## Capital Structure

### Regulatory Capital Instruments

The Company's regulatory capital instruments consist of common stock, preferred stock and subordinated debt. The following table presents components of the Company's capital structure on a Current Expected Credit Losses ("CECL") transitional basis (dollars in millions):

	June 30, 2024
Common stock .....	6
Additional paid-in capital .....	4,603
Retained earnings .....	32,400
Accumulated other comprehensive loss ("AOCI") .....	(398)
Treasury stock .....	(21,064)
Common shareholder's equity .....	15,547
Less: Deductions for goodwill and intangible assets, net of deferred tax liabilities .....	255
Less: Deductions for AOCI related adjustments .....	(398)
Common equity tier 1 ("CET1") .....	15,690
Non-cumulative perpetual preferred stock .....	1,056
Tier 1 capital .....	16,746
Qualifying subordinated debt .....	392
Other elements of tier 2 capital <sup>(1)</sup> .....	1,729
Tier 2 capital .....	2,121
Total capital .....	\$ 18,867

(1) Represents the portion of the allowance for credit losses that is included in Tier 2 capital, which is limited to 1.25% of RWAs.

In accordance with the final rule on the impact of the CECL accounting model on regulatory capital, we have elected to phase in the impact over three years, beginning in 2022. By electing this option, our CET1 capital ratios are higher than they otherwise would have been. The phase-in of the CECL accounting model decreased CET1 by \$1.6 billion as of January 1, 2024. The Company's CET1 capital ratios will continue to be favorably impacted by this election over the phase-in period, which ends December 31, 2024.

Refer to Note 7: Preferred Stock and "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Capital" in the 2Q24 Form 10-Q and Note 12: Common and Preferred Stock in the 2023 Form 10-K for more information related to the terms and conditions of the Company's common and preferred stock.

The following table presents the terms and conditions of the Company's qualifying subordinated debt (dollars in millions):

At June 30, 2024	Issuance Date	Interest Rate	Interest Rate Terms	Maturity	Par
<i>Discover Bank</i>					
Subordinated banknotes due 2028 .....	August 9, 2018	5.97 %	Fixed	August 9, 2028	\$ 500

The subordinated debt is subject to a Basel III provision limiting its amount included on the BHC level. That limitation is imposed on capital instruments issued by a consolidated bank subsidiary of the BHC as the availability of this capital might be limited to the BHC.

## **Regulatory Capital Ratios**

See Note 11: Capital Adequacy in the 2Q24 Form 10-Q and Schedule HC-R in the 2Q24 report form FR Y-9C for the Company's capital ratios and related components as of June 30, 2024.

## **Capital Adequacy**

### **Capital Planning and Management**

The Company's 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.

Under the Federal Reserve's regulatory tailoring framework, DFS is considered a Category IV institution and therefore subject to the least stringent category of enhanced prudential standards for bank holding companies with at least \$100 billion in assets. Among other things, DFS is required to submit to supervisory stress tests every other year rather than annually, is no longer subject to regulations requiring DFS to submit the results of company-run capital stress tests and is no longer subject to the liquidity coverage ratio. However, DFS is still required to submit annual capital plans to the Federal Reserve and remains subject to other core components of enhanced prudential standards, such as risk-management and risk committee requirements and liquidity risk management regulations.

See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Environment and Developments" and "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources" in the 2Q24 Form 10-Q for more information.



## Standardized Approach Risk-Weighted Assets

RWAs are an institution's assets and off-balance-sheet exposures, weighted according to the risk categories prescribed in the Basel III rules. The percentage of RWAs is used to determine minimum capital requirements.

The following table presents components of DFS' RWAs in accordance with the standardized approach, subject to CECL transitional provisions (dollars in millions):

	June 30, 2024
<b>On-balance sheet:</b>	
Exposure to depository institutions and foreign banks .....	\$ 590
Exposures to government-sponsored entities ("GSEs") and public sector entities .....	96
Credit card loan receivables .....	97,930
Personal loan receivables, including private student loans .....	20,329
Residential mortgage exposure .....	6,356
Retail exposure .....	124,615
Past-due exposure <sup>(1)</sup> .....	3,185
Equity exposures .....	526
Other exposures <sup>(2)</sup> .....	9,272
<b>Off-balance sheet:</b>	
Off-balance sheet derivatives .....	—
Off-balance sheet commitments .....	58
Allowance for credit losses excluded from RWAs .....	(6,064)
Total standardized RWAs .....	<u>\$ 132,278</u>

(1) Includes loans that are 90 or more days past-due and non-accruing loans.

(2) Includes \$150 million of business card receivables that are classified as commercial loans under regulatory guidelines.

## Risk-Based Capital Ratios

See Note 11: Capital Adequacy in the 2Q24 Form 10-Q for CET1, tier 1 and total risk-based capital ratios as of June 30, 2024, as calculated under the Basel III standardized approach framework for DFS and Discover Bank.

### Capital Conservation Buffer and Stress Capital Buffer

Under the Basel III rules, the Company and its bank subsidiary must maintain a capital conservation buffer ("CCB") to not be subject to any limitations on distributions of capital or discretionary bonus payments. The CCB is a complementary requirement to the Prompt Corrective Action framework described in the Basel III rules. The CCB is equal to the lowest of: (i) the reported CET1 ratio minus the minimum CET1 ratio; (ii) the reported Tier 1 capital ratio minus the minimum Tier 1 capital ratio; or (iii) the reported total capital ratio minus the minimum total capital ratio.

Federal Reserve rules impose limitations on DFS' capital distributions if the Company does not maintain its risk-based capital ratios above stated regulatory minimum ratios based on the results of supervisory stress tests. DFS is required to assess whether its planned capital actions are consistent with the effective capital distribution limitations that will apply on a pro-forma basis throughout the planning horizon.

The SCB requirement is institution-specific and replaced the fixed 2.5% component of a BHC's CCB. The SCB is calculated as the greater of (i) 2.5% and (ii) the sum of (a) the difference between DFS' actual CET1 ratio at the beginning of the forecast and the projected minimum CET1 ratio based on the Federal Reserve's models in its nine-quarter Severely Adverse stress scenario, plus (b) the sum of the dollar amount of DFS' planned common stock dividend distributions for

each of the fourth through seventh quarters of its nine-quarter capital planning horizon, expressed as a percentage of RWAs. For Category IV firms, including DFS, the Federal Reserve calculates each firm's SCB biennially in even-numbered calendar years, and did so in 2022. Based on the results of the 2022 Comprehensive Capital and Analysis Review ("CCAR") exercise released by the Federal Reserve, DFS' new SCB was set at 2.5%, the lowest possible requirement, effective October 1, 2022, through September 30, 2023. In odd-numbered years, each firm subject to Category IV standards that did not opt-in to such year's supervisory stress tests as part of the Federal Reserve's CCAR process receives an adjusted SCB requirement that is updated to reflect its planned common stock dividends per the firm's annual capital plan. In July 2023, the Federal Reserve publicly disclosed SCB requirements for firms subject to Category IV standards that did not opt-in to this year's stress test. DFS' SCB requirement remains unchanged at 2.5%, effective beginning October 1, 2023 through September 30, 2024. On April 5, 2024, we submitted our 2024 capital plan to the Federal Reserve. On June 26, 2024, the Federal Reserve announced the results of the 2024 CCAR exercise. While the Federal Reserve will not announce final SCB requirements until August, Discover's preliminary SCB has increased to 3.1%. The new SCB would be effective from October 1, 2024, through September 30, 2025, subject to potential recalculation due to the resubmission of our capital plan discussed below.

Under the Basel III rules, a firm must update and resubmit its capital plan under certain circumstances, including a material change in the firm's risk profile, financial condition or corporate structure since its last capital plan submission. On February 19, 2024, Discover and Capital One jointly announced that they entered into a Merger Agreement, under which the companies will combine in an all-stock merger, which we determined required us to resubmit our capital plan. We submitted our updated capital plan on May 3, 2024, and the resubmission process is ongoing. Under the capital plan rule and as a consequence of the resubmission requirement, we must receive prior approval for any dividend or other capital distribution, other than a capital distribution on a newly issued capital instrument.

For additional information related to the results of the Federal Reserve's supervisory stress tests and SCB, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources" in the 2Q24 Form 10-Q.

The SCB final rule does not apply to Discover Bank. The required CCB for Discover Bank continues to be fixed at 2.5%. The Company and its bank subsidiary maintained a buffer of capital sufficient to meet the SCB and CCB requirements, respectively, as of June 30, 2024. See Schedule HC-R Part I in the 2Q24 report form FR Y-9C for DFS' CCB. See Schedule RC-R Part I in the 2Q24 Call Report for Discover Bank's CCB.

The Company's eligible retained income at June 30, 2024, was \$2.1 billion. Except for the prior approval required for any dividend or other capital distribution resulting from our resubmission of our capital plan as discussed above, the Company is not subject to any limitations on distributions and discretionary bonus payments resulting from the CCB framework.

## **Credit Risk: General Disclosures**

### **Credit Risk Management Objectives and Policies**

Credit risk refers to the risk of loss arising from borrower default when borrowers are unable or unwilling to meet their financial obligations to the Company. For all loan types, the Company has established a credit policy and limits that are designed to manage its exposure to credit risk. The Company's credit risk from consumer lending products is generally highly diversified across millions of accounts without significant individual exposures. The Company manages credit risk primarily based on customer segments and product types. See "Business — Credit Risk Management" and "Business — Risk Management" in the 2023 Form 10-K for more information regarding how the Company defines and manages credit and other risks.

### **Delinquent Loans**

See Note 2: Summary of Significant Accounting Policies in the 2023 Form 10-K for the Company's significant accounting policies regarding delinquent loans, non-accrual loans and charge offs of uncollectible amounts.

### **Allowance for Credit Losses**

See Note 2: Summary of Significant Accounting Policies in the 2023 Form 10-K for the Company's significant accounting policies regarding the allowance for credit losses.

## Credit Risk Exposures

The following table presents the major types of on- and off-balance sheet credit exposure and average credit exposure relevant to the Company (dollars in millions):

	June 30, 2024	QTD Average Balance
Cash and cash equivalents <sup>(1)</sup>	\$ 2,947	\$ 2,292
Loans held for investment ("LHFI") <sup>(2)</sup>	\$ 117,504	\$ 126,871
Unused commitments <sup>(3)</sup>	\$ 232,756	\$ 232,966
Debt securities	\$ 13,508	\$ 13,492

(1) Excludes cash held with the Federal Reserve.

(2) Includes credit card, personal and other loans.

(3) Primarily relates to credit cards.

Substantially all of the Company's unused commitments are unconditionally cancellable at any time and receive zero conversion factor for risk-based capital calculations.

The following table presents the geographic distribution of the LHFI and unused commitments (dollars in millions)<sup>(1)</sup>:

At June 30, 2024	LHFI <sup>(2)</sup>	Unused commitments <sup>(3)</sup>
California	\$ 10,818	\$ 20,682
Texas	10,531	19,079
Florida	8,704	16,874
New York	7,375	14,567
Illinois	5,627	12,288
Pennsylvania	5,509	12,342
Ohio	4,637	10,182
New Jersey	4,112	8,363
Georgia	3,961	6,636
North Carolina	3,187	5,887
Other	53,043	105,856
Total	<u>\$ 117,504</u>	<u>\$ 232,756</u>

(1) The company originates loans throughout the U.S. The geographic region is classified based on the domicile of the borrower.

(2) Includes credit card, personal and other loans.

(3) Primarily relates to credit cards.

All debt securities held by the Company were issued by domestic parties. The Company held \$51 million of cash and cash equivalents in accounts outside the U.S. as of June 30, 2024.

The following table presents the distribution of credit exposures by counterparty type (dollars in millions):

At June 30, 2024	Retail	Sovereign (including GSEs)	Banks & Brokerage companies <sup>(1)</sup>	Other
Cash and cash equivalents <sup>(1)</sup> .....	\$ —	\$ —	\$ 2,947	
LHFI <sup>(2)</sup> .....	\$ 117,303			\$ 201
Unused commitments <sup>(3)</sup> .....	\$ 231,957			\$ 799
Debt securities .....		\$ 13,508		
Loans 90 or more days past-due and non-accruing .....	\$ 62	\$ —	\$ —	\$ —
Loans 90 or more days past-due and accruing .....	\$ 1,840	\$ —	\$ —	\$ 1

(1) Excludes cash held with the Federal Reserve.

(2) Includes credit card, personal and other loans.

(3) Primarily relates to credit cards.

The following table presents the remaining contractual maturity delineation of the LHFI portfolio<sup>(1)</sup> (dollars in millions):

	June 30, 2024
One year or less .....	\$ 91,325
Over one year through five years .....	\$ 16,192
Over five years .....	\$ 9,715

(1) Includes fixed-rate credit cards in the "over one year through five years" classification per Call Report guidelines and excludes loans in non-accrual status.

See the following references to the Company's 2Q24 Form 10-Q for quantitative information regarding credit risk exposures, which are presented in accordance with U.S. GAAP.

#### Loan Receivables

- See Note 3: Loan Receivables for information on outstanding loans, non-accrual loans, delinquent loans, as well as charge-offs during the period. The Company does not identify past-due loans by significant geographic area.

#### Allowance for Credit Losses

- See Note 3: Loan Receivables for a reconciliation of changes in the allowance for credit losses.

### Counterparty Credit Risk-Related Exposures: General Disclosures

#### Counterparty Credit Risk Exposures

With respect to derivatives, counterparty credit risk is the risk that the counterparty to a derivative transaction could default before the final settlement of the transaction's cash flows. The Company's counterparty credit risk from derivatives arises primarily from interest rate swap transactions and foreign exchange forward transactions. For non-cleared transactions, the Company has master netting arrangements and minimum collateral posting thresholds with its counterparties for its fair value and cash flow hedge interest rate swaps and foreign exchange forward contracts. For cleared transactions, the Company trades through clearing members of a central counterparty ("CCP") exchange such that all positions traded through the CCP clearing member are netted and collateralized pursuant to the rules of the exchange. As a result, certain cash collateral amounts associated with derivative positions that are cleared through a CCP exchange are legally characterized as settlement of the derivative positions and are reflected as offsets to the associated derivatives balances recorded in other assets or accrued expenses and other liabilities, instead of as collateral in other assets or deposits. For more information on the Company's derivatives, including the counterparty credit risk-related exposures, see Note 15: Derivatives and Hedging Activities in the 2Q24 Form 10-Q.

With respect to securities repurchase and reverse repurchase transactions, counterparty credit risk is the risk that the counterparty to a transaction could default before the securities and cash (plus interest) in the transaction have been returned to their original owners. For securities repurchase and reverse repurchase transactions, the Company's counterparty credit risk arises from its use of agreements with major broker-dealer counterparties or central banks using primarily U.S. Treasury and/or agency securities as collateral.

### **Methodology Used to Assign Counterparty Credit Limits**

The process for approving a counterparty's credit risk exposure limit is guided by (i) core credit policies, (ii) procedures and standards and (iii) the experience and judgment of credit risk professionals. The process applies to all investment and hedging activities conducted by the Company's Treasury group and includes determining the maximum potential exposure to each counterparty after considering market volatility, netting agreements and collateral support as appropriate.

Internal ratings are assigned to each counterparty and reflect a range of factors, including the counterparty's financial condition, the strength of its management, the counterparty's business profile and the regulatory environment facing the counterparty. The Company considers these factors in setting counterparty credit exposure limits, which drive internal approval levels.

Credit risk analysts conduct daily monitoring of exposures versus limits with any resulting issues escalated to risk officers and senior management in accordance with established policies.

### **Policies for Securing, Valuing and Managing Collateral and Establishing Credit Reserves**

The Company's policies and procedures cover the management and governance of financial assets (including securing and valuing collateral) utilized to mitigate counterparty credit risk. Specifically, the Company's Corporate Risk Management group considers standard eligibility criteria and market value haircuts for any collateral used to reduce estimated net exposures in the Company's transactions. In addition, industry-standard legal agreements combined with internal reviews for legal enforceability are employed to ensure that the Company's rights to collateral are appropriately protected.

The Company monitors the market value of the collateral regularly where the collateral offsets the estimated exposure. The Company's Treasury group has procedures for managing margin calls to maintain an appropriate level of collateral coverage in light of market value fluctuations and CCP exchange rules. The Company reconciles trades daily, consistent with regulatory guidance and industry best practices, and margin dispute processes are in place. These margining processes and the regular monitoring of exposures mitigate the counterparty credit risk arising from derivative transactions and securities repurchase and reverse repurchase transactions.

### **Primary Types of Collateral for Derivatives Exposures**

Cleared transactions are cash-settled daily, with cash and U.S. Treasury securities used to meet daily margin requirements, per CCP exchange rules. The net open exposure of non-cleared derivative transactions is secured using cash collateral and U.S. Treasury securities.

### **Credit Risk Mitigation**

As part of its risk management activities, the Company uses various risk mitigants to manage portions of the credit risk in its portfolios. Credit risk mitigation is important to the Company in effectively managing its credit risk exposures. Credit card receivables comprise a majority of the Company's assets, with unfunded commitments that are unconditionally cancellable.

Loans secured by first lien 1-4 family residential properties is the sole asset category of the Company that benefits from collateral to reduce capital requirements. As of June 30, 2024, RWAs were reduced by \$711 million due to collateral held against those loans, which represented 0.5% of the total RWAs and had an immaterial impact on the Company's capital ratios.

As of June 30, 2024, the Company does not utilize credit derivatives as a risk mitigation tool.

## Securitization

### Securitization Activities

The Company engages in credit card and private student loan securitization activities. The Company's securitizations are accounted for as secured borrowings, and the related trusts are treated as consolidated subsidiaries of the Company. The assets of the Company's consolidated securitization trusts are restricted from being sold or pledged as collateral for other borrowings. The cash flows from these restricted assets may be used only to pay obligations of the trusts. The related debt issued by all securitization trusts is reported primarily in long-term borrowings.

The Company accesses the term asset securitization market through the Discover Card Master Trust I ("DCMT") and the Discover Card Execution Note Trust ("DCENT"). Credit card loan receivables are transferred into DCMT and beneficial interests in DCMT are transferred into DCENT. DCENT issues debt securities to investors. Credit card and private student loan trust receivables underlying third-party investors' interests are recorded in credit card loan receivables and private student loan receivables, respectively. See Note 4: Credit Card and Private Student Loan Securitization Activities in the 2Q24 Form 10-Q for more information on the Company's credit card and private student loan securitization activities.

The total outstanding principal amount of assets securitized by the Company does not meet operational criteria as defined in the Basel III rules. As a result, the underlying assets are reconsolidated in the balance sheet and accordingly risk-weighted based on their balance sheet classification for Basel III purposes. In addition, the Company did not hold investments in asset-backed securities subject to Basel III securitization disclosure requirements as of June 30, 2024. As a result, Table 8 of disclosure requirements under section 217.63 does not apply to the Company at this time.

### Equities Not Subject to Market Risk Rule

#### Overview

The Company makes investments in equities with objectives of (i) fostering strategic relationships, (ii) fulfilling Community Reinvestment Act requirements and (iii) generating capital gains.

The following table presents the carrying value and fair value of the Company's equity investments (dollars in millions):

At June 30, 2024	Carrying Value	Fair Value
Equity investments	\$ 590	\$ 590

There were no cumulative realized gains or losses during the three months ended June 30, 2024. There were no net unrealized gains or losses that have not been recognized on the consolidated statement of financial condition or through earnings or that were included in tier 1 and tier 2 capital.

Refer to Note 14: Fair Value Measurements in the 2Q24 Form 10-Q for more information related to the Company's methodologies regarding the valuation of equity investments. Refer to Note 2: Investments in the 2Q24 Form 10-Q for more information related to the Company's accounting for equity investments.

### Risk Weighting

The Company utilizes different approaches in calculating RWAs for equity exposures not subject to market risk capital rules. Under the Simplified Risk-Weight Approach ("SRWA"), different types of equity exposures are assigned specific risk weights between 0 percent and 600 percent. The adjusted carrying value for each type of equity exposure is multiplied by the prescribed risk weight. The adjusted carrying value for an on-balance sheet exposure is the carrying value of the exposure. Although the SRWA assigns specific risk weights to different types of equity exposures, the final rule allows "non-significant equity exposures" to be risk-weighted at 100 percent. Equity investments are non-significant if the aggregate adjusted carrying value of the exposures does not exceed 10 percent of a banking organization's total capital. As DFS' total equity exposure was below the 10 percent threshold as of June 30, 2024, the Company assigned a risk-weighting of 100 percent for each non-significant equity exposure.

The Alternative Modified Look-Through Approach is used to calculate RWA amounts for equity exposures to investment funds. Using the Alternative Modified Look-Through Approach, the adjusted carrying value of an equity exposure to an investment fund is assigned on a pro-rata basis to the different risk weight categories based on the

investment limits in the fund's prospectus, partnership agreement, or similar contract that defines the fund's permissible investments. It is assumed the fund invests to the maximum extent permitted under its investment limits in the exposure type with the highest applicable risk weight and continues to make investments in the order of the exposure type with the next highest applicable risk weight until the maximum total investment is reached.

The following table presents the Company's equity exposures not subject to the Basel III market risk capital rule, using the SRWA and the Alternative Modified Look-Through Approach (dollars in millions):

<u>At June 30, 2024</u>	<u>Risk Weight %</u>	<u>Exposure</u>	<u>RWAs</u>
Community Development Equity Exposure .....	100%	\$ 463	\$ 463
Non-Publicly Traded Equity Exposures .....	100%	47	47
Federal Home Loan Bank Exposure .....	20%	47	9
Modified Look-Through .....		33	7
Total equity exposure not subject to the Basel III market risk capital rule .....		<u>\$ 590</u>	<u>\$ 526</u>

### Interest Rate Risk for Non-Trading Activities

See "Quantitative and Qualitative Disclosures About Market Risk" in the 2Q24 Form 10-Q for information on the Company's interest rate risk related to non-trading activities.