NORTHERN TRUST CORP
Form 10-K
February 26, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2012

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. 0-5965

NORTHERN TRUST CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**36-2723087**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
50 South La Salle Street Chicago, Illinois	**60603**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (312) 630-6000

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

Title of Each Class	Name of Each Exchange On Which Registered
Common Stock, $1.66 2/3 Par Value	**The NASDAQ Stock Market**

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

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

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

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

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

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

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 definitions of accelerated filer , large 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 ¨	Smaller reporting company ¨

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

The aggregate market value of the Common Stock as of June 29, 2012 (the last business day of the registrant s most recently completed second quarter), based upon the last sale price of the Common Stock at June 29, 2012 as reported by The NASDAQ Stock Market, held by non-affiliates was approximately $11,068,598,277. Determination of stock ownership by non-affiliates was made solely for the purpose of responding to this requirement and the registrant is not bound by this determination for any other purpose.

At February 18, 2013, 239,157,282 shares of Common Stock, $1.66 2/3 par value, were outstanding.

Portions of the following documents are incorporated by reference:

Annual Report to Stockholders for the Fiscal Year Ended December 31, 2012 Part I and Part II

2013 Notice and Proxy Statement for the Annual Meeting of Stockholders to be held on April 16, 2013 Part III

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Northern Trust Corporation

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d)

of the Securities Exchange Act of 1934

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PART I

Item 1 Business

NORTHERN TRUST CORPORATION

Northern Trust Corporation (Corporation) is a financial holding company that is a leading provider of asset servicing, fund administration, asset management, fiduciary and banking solutions for corporations, institutions, families and individuals worldwide. The Corporation conducts business through various U.S. and non-U.S. subsidiaries, including The Northern Trust Company (Bank). The Corporation was originally formed as a holding company for the Bank in 1971. The Corporation has a network of offices in 18 U.S. states, Washington, D.C., and 16 international locations in North America, Europe, the Middle East, and the Asia Pacific region. At December 31, 2012, the Corporation had consolidated total assets of $97.5 billion and stockholders equity of $7.5 billion.

The Bank is an Illinois banking corporation headquartered in the Chicago financial district and the Corporation s principal subsidiary. Founded in 1889, the Bank conducts its business through its U.S. operations and its various U.S. and non-U.S. branches and subsidiaries. At December 31, 2012, the Bank had consolidated assets of $97.1 billion and common equity capital of $7.2 billion.

The Corporation expects that, although the operations of other banking and non-banking subsidiaries will continue to be of increasing significance, the Bank will in the foreseeable future continue to be the major source of the Corporation s consolidated assets, revenues, and net income. Except where the context otherwise requires, the term Northern Trust refers to Northern Trust Corporation and its subsidiaries on a consolidated basis. A complete list of the Corporation s direct and indirect subsidiaries is filed as Exhibit 21 to this Annual Report on Form 10-K and incorporated into this Item by reference.

BUSINESS UNITS

Under the leadership of Frederick H. Waddell, the Chairman of the Board and Chief Executive Officer of the Corporation, Northern Trust organizes its services globally around its two client-focused principal business units: Corporate and Institutional Services (C&IS) and Personal Financial Services (PFS). Two other business units provide services to the two principal business units: Northern Trust Global Investments (NTGI), which provides investment management, and Operations and Technology (O&T), which provides operating and systems support.

Financial information regarding the Corporation and its business units is included in the Corporation s Annual Report to Stockholders for the year ended December 31, 2012. In particular, for a discussion of significant developments in the business of the Corporation, and the impact on the financial results of the Corporation and its business units for the fiscal year ended December 31, 2012, you are urged to review the section entitled Consolidated Results of Operations on pages 20 through 28 of Management s Discussion and Analysis of Financial Condition and Results of Operations of the Corporation s Annual Report to Stockholders for the year ended December 31, 2012, which is incorporated herein by reference.

The following is a brief summary of each business unit s activities.

Corporate & Institutional Services

C&IS is a leading global provider of asset servicing, securities lending, brokerage, banking and related services to corporate and public retirement funds, foundations, endowments, fund managers, insurance companies, sovereign wealth and government funds. Asset servicing and related services encompass a full range of industry leading capabilities including but not limited to: global master trust and custody, trade settlement, and reporting; fund administration; cash management; investment risk and performance analytical services; investment operations outsourcing; and transition management and commission recapture. Client relationships are managed through the Bank and the Bank s and the Corporation s other subsidiaries, including support from international locations in North America, Europe, the Middle East, and the Asia Pacific region. C&IS also executes related foreign exchange transactions from offices located in the United States, United Kingdom, and Singapore. At December 31, 2012, total C&IS assets under custody were $4.4 trillion and assets under management were $561.2 billion.

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Personal Financial Services

PFS provides personal trust, investment management, custody, and philanthropic services; financial consulting; guardianship and estate administration; brokerage services; and private and business banking. PFS focuses on high net worth individuals and families, business owners, executives, professionals, retirees, and established privately held businesses in its target markets. PFS also includes the Global Family Office, which provides customized products and services to meet the complex financial needs of individuals and family offices in the United States and throughout the world with assets typically exceeding $200 million.

PFS is one of the largest providers of personal trust services in the United States, with $446.3 billion in assets under custody and $197.7 billion in assets under management at December 31, 2012. PFS services are delivered through a network of offices in 18 U.S. states and Washington, D.C., as well as offices in London and Guernsey.

Northern Trust Global Investments

NTGI, through various subsidiaries of the Corporation, provides a broad range of asset management and related services and products to clients around the world, including clients of C&IS and PFS. Clients include institutional and individual separately managed accounts, bank common and collective funds, registered investment companies, exchange traded funds, non-U.S. collective investment funds, and unregistered private investment funds. NTGI offers both active and passive equity and fixed income portfolio management, as well as alternative asset classes (such as private equity and hedge funds of funds) and multi-manager advisory services and products. NTGI s activities also include overlay services and other risk management services. NTGI s business operates internationally through subsidiaries and distribution arrangements.

Operations and Technology

O&T supports all of Northern Trust s business activities, including the processing and product management activities of C&IS, PFS, and NTGI. These activities are conducted principally in the operations and technology centers in Chicago, London, and Bangalore.

GOVERNMENT MONETARY AND FISCAL POLICIES

The earnings of Northern Trust are affected by numerous external influences. Chief among these are general economic conditions, both domestic and international, and actions that governments and their central banks take in managing their economies. These general conditions affect all of Northern Trust s businesses, as well as the quality, value, and profitability of their loan and investment portfolios.

The Board of Governors of the Federal Reserve System (Federal Reserve Board) is an important regulator of U.S. economic conditions and has the general objective of promoting orderly economic growth in the United States. Implementation of this objective is accomplished by the Federal Reserve Board s open market operations in United States Government securities, its setting of the discount rate at which member banks may borrow from Federal Reserve Banks, and its changes in the reserve requirements for deposits. The policies adopted by the Federal Reserve Board may strongly influence interest rates and hence what banks earn on their loans and investments and what they pay on their savings and time deposits and other purchased funds. Fiscal policies in the United States and abroad also affect the composition and use of Northern Trust s resources.

COMPETITION

The businesses in which Northern Trust operates are very competitive. Competition is provided by both unregulated and regulated financial services organizations, whose products and services span the local, national, and global markets in which Northern Trust conducts operations.

Northern Trust s principal business strategy is to provide quality financial services to targeted market segments in which it believes it has a competitive advantage and favorable growth prospects. As part of this strategy, Northern Trust seeks to deliver a level of service that distinguishes it from its competitors. In addition, Northern Trust emphasizes the development and growth of recurring sources of fee-based income and is one of a select group of major bank holding companies in the United States that generates more revenues from fee-based services than from net interest income. Northern Trust seeks to develop and expand its recurring fee-based revenue by identifying selected markets with good growth characteristics and providing a high level of individualized service to clients in those markets. Northern Trust also seeks to preserve its asset quality through established credit review procedures and to maintain a conservative balance sheet. Finally, Northern Trust seeks to operate with a strong management team that includes senior officers having broad experience and long tenures.

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Commercial banks, savings banks, savings and loan associations, and credit unions actively compete for deposits, and money market funds and investment banking firms offer deposit-like services. These institutions, as well as consumer and commercial finance companies, national retail chains, factors, insurance companies, and pension trusts, are important competitors for various types of loans. Issuers of commercial paper compete actively for funds and reduce demand for bank loans. For personal and corporate trust services and investment counseling services, trust companies, investment banking firms, insurance companies, investment counseling firms, and others offer active competition.

REGULATION AND SUPERVISION

Financial Holding Company Regulation

Under U.S. law, the Corporation is a bank holding company that has elected to be a financial holding company under the Bank Holding Company Act of 1956, as amended (BHCA). Consequently, the Corporation and its business activities throughout the world are subject to the supervision, examination, and regulation of the Federal Reserve Board. The BHCA and other federal laws subject bank and financial holding companies to particular restrictions on the types of activities in which they may engage and to a range of supervisory requirements, including regulatory enforcement actions for violations of laws and regulations. Supervision and regulation of bank holding companies, financial holding companies, and their subsidiaries are intended primarily for the protection of depositors and other clients of banking subsidiaries, the Deposit Insurance Fund (DIF) of the Federal Deposit Insurance Corporation (FDIC), and the banking system as a whole, not for the protection of stockholders or other non-depository creditors.

Under the BHCA, bank holding companies and their banking subsidiaries are generally limited to the business of banking and activities closely related or incidental to banking. As a financial holding company, the Corporation is permitted to engage in other activities that the Federal Reserve Board, working with the Secretary of the Treasury, determines to be financial in nature, incidental to an activity that is financial in nature, or complementary to a financial activity and that do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally, or to acquire shares of companies engaged in such activities. Activities defined to be financial in nature include: providing financial or investment advice; securities underwriting and dealing; insurance underwriting; and making merchant banking investments in commercial and financial companies, subject to significant limitations. They also include activities previously determined by the Federal Reserve Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. The Corporation may not, however, directly or indirectly acquire the ownership or control of more than 5% of any class of voting shares, or substantially all of the assets, of a bank holding company or a bank, without the prior approval of the Federal Reserve Board.

In order to maintain the Corporation s status as a financial holding company, the Corporation s insured depository institution subsidiary, the Bank, must remain well capitalized and well managed under applicable regulations, and must have received at least a satisfactory rating in its most recent examination under the Community Reinvestment Act (CRA). In addition, the Corporation must also be and remain well-capitalized and well managed in order to retain its status as a financial holding company. Failure to meet one or more of these requirements would mean, depending on the requirements not met, that the Corporation could not undertake new activities, continue certain activities, or make acquisitions other than those permitted generally for bank holding companies.

Subsidiary Regulation

The Bank is a member of the Federal Reserve System, its deposits are insured by the FDIC up to the maximum authorized limit, and it is subject to regulation by both these agencies. The Bank, as an Illinois banking corporation, is also subject to Illinois state laws and regulations and to examination and supervision by the Division of Banking of the Illinois Department of Financial and Professional Regulation. The Bank is registered as a government securities dealer in accordance with the Government Securities Act of 1986. As a government securities dealer, its activities are subject to the rules and regulations of the Department of the Treasury. The Bank is also registered as a transfer agent with the Federal Reserve Board and is therefore subject to the rules and regulations of the Federal Reserve Board in this area.

The Corporation s nonbanking affiliates are all subject to examination by the Federal Reserve Board. Its broker-dealer subsidiary is registered with the Securities and Exchange Commission (SEC) and is a member of the Financial Industry Regulatory Authority, subject to the rules and regulations of both of these bodies. Several subsidiaries of the Corporation are registered with the SEC under the Investment Advisers Act of 1940 and are subject to that act and the rules and regulations promulgated thereunder. Other subsidiaries are regulated by state banking departments in various states. The Bank and other subsidiaries of the Corporation act as investment advisers to several mutual funds and other asset managers which are subject to regulation by the SEC under the Investment Company Act of 1940.

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Functional Regulation

Federal banking law has established a system of federal and state supervision and regulation based on functional regulation, meaning that primary regulatory oversight for a particular activity generally resides with the federal or state regulator designated as having the principal responsibility for that activity. Banking is supervised by federal and state banking regulators, insurance by state insurance regulators, and securities activities by the SEC and state securities regulators.

A significant component of the functional regulation relates to the application of federal securities laws and SEC oversight of some bank securities activities. Generally, banks may conduct securities activities without broker-dealer registration only if the activities fall within a set of activity-based exemptions designed to allow banks to conduct only those activities traditionally considered to be primarily banking or trust activities. Securities activities outside these exemptions, as a practical matter, need to be conducted by a registered broker-dealer affiliate. The Investment Advisers Act of 1940 requires the registration of any bank or separately identifiable division of the bank that acts as investment adviser for mutual funds. The Corporation believes that it has taken the necessary actions to comply with these requirements of federal law.

Non-U.S. Regulation

The increasingly important activities of the Corporation s subsidiaries outside the U.S. are subject to regulation and supervision by a number of non-U.S. regulatory agencies. Subsidiaries conducting banking, fund administration and asset servicing businesses in the United Kingdom, for example, are subject to regulation by and supervision of the Financial Services Authority (FSA), and are authorized to conduct such activities pursuant to the U.K. Financial Services and Markets Act of 2000. The FSA exercises broad supervisory and disciplinary powers that include the power to temporarily or permanently revoke authorization to conduct a regulated business upon breach of the relevant regulations, suspend registered employees, and impose censures and fines on both regulated businesses and their registered employees. The non-U.S. subsidiaries of the Corporation and branches of the Bank outside the U.S. are subject to the laws and regulatory authorities of the jurisdictions in which they operate. Additionally, the Corporation s subsidiary banks located outside the U.S. are subject to regulatory capital requirements in the jurisdictions in which they operate. As of December 31, 2012, each of the Corporation s non-U.S. banking subsidiaries had capital ratios above their specified minimum requirements. As is the case in the U.S., European regulatory authorities are introducing regulatory change in a wide variety of areas. For example, new regulations issued by European regulators through the Undertaking for Collective Investment in Transferable Securities (UCITS) IV Directive directly and indirectly affect depositary, fund management, and fund administration businesses. European authorities are in the process of implementing the Alternative Investment Fund Managers Directive which will affect the duties of depositaries, European Union (EU) and non-EU fund managers and non-UCITS funds. European regulatory authorities are also putting forward proposals through the Markets in Financial Instruments Directive 2, European Market Infrastructure Regulation and Market Abuse Regulation proposals which deal with derivatives trading and clearing, pre and post trade transparency, investor protection issues and overall market orderliness. These actual and proposed regulatory changes have impacted, and will impact, the business that the Bank and its non-U.S. subsidiaries conduct in the European Union.

The Dodd-Frank Act

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) is having a broad impact on the financial services industry and imposes significant new regulatory and compliance requirements, including the designation of certain financial companies as systemically important financial institutions (SIFIs), the imposition of increased capital, leverage, and liquidity requirements, and numerous other provisions designed to improve supervision and oversight of, and strengthen safety and soundness within, the financial services sector. Additionally, the Dodd-Frank Act establishes a new framework of authority to conduct systemic risk oversight within the financial system to be distributed among new and existing federal regulatory agencies, including the Financial Stability Oversight Council (FSOC), the Federal Reserve Board, the Office of the Comptroller of the Currency (OCC), and the FDIC.

The following items provide a brief description of certain provisions of the Dodd-Frank Act that are most relevant to the Corporation and its banking subsidiaries.

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Heightened Prudential Requirements. The Dodd-Frank Act imposes heightened prudential requirements on U.S. bank holding companies with at least $50 billion in total consolidated assets, including the Corporation, and on large financial companies and nonbank financial companies that the FSOC determines should be subject to Federal Reserve Board supervision. These companies are referred to as systemically important financial institutions, or SIFIs. The heightened prudential standards include more stringent risk-based capital, leverage, liquidity and risk-management requirements than those applied to other bank holding companies or other financial companies. The Federal Reserve Board and the FSOC will also have the discretion to require these companies to limit their short-term debt, to issue contingent capital instruments, and to provide enhanced public disclosures. SIFIs will also be subject to periodic stress tests to evaluate capital adequacy and liquidity in adverse economic conditions. Heightened prudential standards may be applied on a graduated basis using the factors included in the FSOC systemic determination standards. On December 20, 2011, the Federal Reserve Board requested public comments on proposed rules that would implement the enhanced prudential standards required to be established under section 165 of the Dodd-Frank Act and the early remediation requirements established under section 166 of the Dodd-Frank Act. In addition, covered companies, including the Corporation, must prepare and file credit exposure reports and limit their aggregate credit exposures (broadly defined) to any unaffiliated company to 25 percent of the capital stock and surplus of the covered company.

Resolution Planning. As required by the Dodd-Frank Act, the Federal Reserve and FDIC have jointly issued a final rule that requires certain organizations, including each BHC with consolidated assets of $50 billion or more, to submit periodically to regulators a resolution plan for its rapid and orderly resolution in the event of material financial distress or failure. The Corporation s resolution plan must, among other things, ensure that our depository institution subsidiaries are adequately protected from risks arising from our other subsidiaries. The final rule sets specific standards for the resolution plans, including requiring a strategic analysis of the plan s components, a description of the range of specific actions the company proposes to take in resolution, and a description of the company s organizational structure, material entities, interconnections and interdependencies, and management information systems, among other elements. In addition, the FDIC has issued a final rule that requires insured depository institutions with $50 billion or more in total assets, such as the Bank, to submit to the FDIC periodic plans for resolution in the event of the institution s failure. The rule requires these insured institutions to submit a resolution plan that will enable the FDIC, as receiver, to resolve the bank in a manner that ensures that depositors receive access to their insured deposits within one business day of the institution s failure, maximizes the net-present-value return from the sale or disposition of its assets, and minimizes the amount of any loss to be realized by the institution s creditors. The final rule also sets specific standards for the resolution plans, including requiring a strategic analysis of the plan s components, a description of the strategies for achieving the least costly resolution, and analyses of the financial company s organization, material entities, interconnections and interdependencies, and management information systems, among other elements. Our initial plans are required to be submitted to the regulators by December 31, 2013.

Mortgage Loan Origination and Risk Retention. The Dodd-Frank Act imposes new standards for mortgage loan originations on all lenders, including banks and thrifts. Most significantly, the new standards prohibit the Corporation s subsidiaries from making a residential mortgage loan without verifying a borrower s ability to repay, limit the total points and fees that the Corporation s subsidiaries and/or a mortgage broker may charge on conforming and jumbo loans to 3% of the total loan amount, and prohibit certain prepayment penalty practices. Also, the Dodd-Frank Act, in conjunction with the Federal Reserve Board s final rule on loan originator compensation prohibits certain compensation payments to loan originators and steering consumers to loans not in their interest because it will result in greater compensation for a loan originator. These standards will result in a myriad of new system, pricing, and compensation controls in order to ensure compliance and to decrease repurchase requests and foreclosure defenses.

Proprietary Trading and Certain Relationships with Hedge Funds and Private Equity Funds. The Dodd-Frank Act adopts the so-called Volcker Rule which, subject to a two-year transition period and certain exceptions, became effective on July 21, 2012 and prohibits a banking entity from engaging in proprietary trading, which is defined as engaging as principal for the trading account of the banking entity in securities or other instruments, as determined by federal regulators. Certain forms of proprietary trading may qualify as permitted activities, and thus not be subject to the ban on proprietary trading, such as market-making-related activities , risk-mitigating hedging activities , and trading in U.S. government or agency obligations, certain other U.S., state or municipal obligations, and the obligations of Fannie Mae, Freddie Mac or Ginnie Mae. Additionally, subject to a transition period and certain exceptions, the rule restricts a banking entity from sponsoring or investing in certain private funds. While a banking entity may organize and offer certain private funds if certain conditions are met, it may not acquire or retain an equity partnership or other ownership interest in such private funds except for certain limited investments.

A banking entity that sponsors or invests in certain private funds is also restricted from providing credit or other support to the fund or permitting the fund to use the name of the bank. After the conformance period commencing July 21, 2012, the Volcker Rule prohibitions and restrictions will apply to banking entities, including the Corporation, the Bank and their affiliates, unless an exception applies. In October 2011, the OCC, Federal Reserve Board, the FDIC, and the SEC, in consultation with the Commodity Futures Trading Commission (CFTC), jointly released a notice of proposed rulemaking implementing the Volcker Rule limitations of the Dodd-Frank Act. To date, no final rule has been issued. In light of the complexity of the proposed regulation and the substantial number of comments submitted, the Corporation cannot fully assess the impact of the Volcker Rule on its business until final rules are adopted.

Swaps and Other Derivatives. Title VII of the Dodd-Frank Act (Title VII) imposes a new regulatory structure on the over-the-counter derivatives market, including requirements for clearing, exchange trading, capital, margin, reporting, and recordkeeping. In addition, certain swaps and other derivatives activities are required to be pushed out of insured depository institutions and conducted in separately capitalized non-bank affiliates. Title VII also will require certain persons to register as a major swap participant or a swap dealer. The CFTC, SEC and other U.S. regulators have adopted and are still in the process of adopting regulations to implement Title VII. It is anticipated that this rulemaking process will further clarify, among other things, reporting and recordkeeping obligations, margin and capital requirements, the scope of registration requirements, and what swaps are required to be centrally cleared and exchange-traded. Rules will also be issued to enhance the oversight of clearing and trading entities.

Consumer Financial Protection. The Dodd-Frank Act establishes a new independent Consumer Financial Protection Bureau (CFPB) within the Federal Reserve System. The CFPB is tasked with establishing and implementing rules and regulations under certain federal consumer protection laws with respect to the conduct of providers of certain consumer financial products and services. The CFPB has rulemaking authority over many of the statutes governing financial products and services offered to consumers. For banking organizations with assets of $10 billion or more, including the Bank, the CFPB has exclusive rule making and examination, and primary enforcement, authority under federal consumer financial laws. In addition, the Dodd-Frank Act permits states to adopt consumer protection laws and regulations that are stricter than those regulations promulgated by the CFPB. This new federal and state regulatory framework may result in significant new regulatory requirements applicable to the Corporation and its bank subsidiaries in respect of consumer financial products and services, with potentially significant increases in compliance costs.

Incentive Compensation Arrangements. The Dodd-Frank Act requires federal regulators to prescribe regulations or guidelines regarding incentive-based compensation practices at certain large financial institutions. On April 14, 2011, federal regulators including the FDIC, the Federal Reserve Board and the SEC, issued a proposed rule which, among other things, would require certain executive officers of covered financial institutions with total consolidated assets of $50 billion or more, including the Corporation, to defer at least 50% of their annual incentive-based compensation for a minimum of three years. No final rule has been issued to date.

The requirements of the Dodd-Frank Act will be implemented pursuant to regulations over the course of several months or years. Given the uncertainty associated with future regulatory actions, the full impact such requirements will have on the Corporation s operations is unclear. The changes resulting from the Dodd-Frank Act may impact the profitability of the Corporation s banking subsidiaries, require changes to certain of the Corporation s business practices, impose upon the Corporation more stringent capital, liquidity and leverage requirements, and could adversely affect certain of the Corporation s business activities. These changes may also require the Corporation and its subsidiaries to invest significant management attention and resources to evaluate and make any changes necessary to comply with new requirements.

Holding Company Support and Cross-Guarantees under the FDIA

Under the FDIA, when two or more insured depository institutions are under common control, each of those depository institutions may be liable for any loss incurred, or expected to be incurred, by the FDIC in connection with the default of any of the others. Each also may be liable for any assistance the FDIC provides to the other institutions. Default means the appointment of a conservator or receiver for the institution.

The Dodd-Frank Act amends the FDIA to obligate the Federal Reserve Board to require bank holding companies and savings and loan holding companies to serve as a source of financial strength for any subsidiary depository institution. The appropriate federal banking agency for such a depository institution may require reports from companies that own the insured depository institution to assess their ability to serve as a source of strength and to enforce compliance with the source-of-strength requirements. The term source of financial strength is defined as the ability of a company to provide financial assistance to its insured depository institution subsidiaries in the event of financial distress at such subsidiaries. Under this requirement, the Corporation in the future could be required to provide financial assistance to the Bank should the Bank experience financial distress. The Dodd-Frank Act statutory requirements became effective on July 21, 2011. Although the appropriate federal banking agencies were required by the Dodd-Frank Act to jointly adopt implementing regulations by July 21, 2011, to date no final regulations have been adopted.

This cross-guarantee liability for a loss at a commonly controlled institution would be subordinated in right of payment to deposit liabilities, secured obligations, any other general or senior liability, and any obligation subordinated to depositors or other general creditors, other than obligations owed to any affiliate of the depository institution (with certain exceptions).

Payment of Dividends

The Corporation is a legal entity separate and distinct from its subsidiaries. The principal source of funds for the Corporation is dividends from the Bank. As a result, the Corporation s ability to pay dividends on its common stock will depend primarily on the ability of the Bank to pay dividends to the Corporation in amounts sufficient to service its obligations. Dividend payments from the Bank are subject to Illinois law and to regulatory limitations, generally based on capital levels and current and retained earnings, imposed by various regulatory agencies with authority over the Bank. The ability of the Bank to pay dividends is also subject to regulatory restrictions if paying dividends would impair its profitability, financial condition or cash flow requirements.

The Federal Reserve Board has issued a policy statement with regard to the payment of cash dividends by bank holding companies. The policy statement provides that, as a matter of prudent banking, a bank holding company should not maintain a rate of cash dividends unless its net income available to common stockholders has been sufficient to fully fund the dividends, and the prospective rate of earnings retention appears to be consistent with the holding company s capital needs, asset quality, and overall financial condition. Accordingly, without Federal Reserve Board approval, a bank holding company cannot pay cash dividends that exceed its net income, and cash dividends cannot be funded in ways that weaken the bank holding company s financial health, such as by borrowing.

Various federal and state statutory provisions limit the amount of dividends the Bank can pay to the Corporation without regulatory approval. Approval of the Federal Reserve Board is required for payment of any dividend by a state chartered bank that is a member of the Federal Reserve System if the total of all dividends declared by the bank in any calendar year would exceed the total of its retained net income (as defined by regulatory agencies) for that year combined with its retained net income for the preceding two years. In addition, a state member bank may not pay a dividend in an amount greater than its undivided profits, as defined, without regulatory and stockholder approval.

The Bank is also prohibited under federal law from paying any dividends if the Bank is undercapitalized or if the payment of the dividends would cause the Bank to become undercapitalized. In addition, the federal regulatory agencies are authorized to prohibit a bank or bank holding company from engaging in an unsafe or unsound banking practice. The payment of dividends could, depending on the financial condition of the Bank, be deemed to constitute an unsafe or unsound practice. The Dodd-Frank Act and Basel III (as described below) impose additional restrictions on the ability of banking institutions to pay dividends.

Bank holding companies domiciled in the U.S. with total consolidated assets of $50 billion or more, including the Corporation, must submit annual capital plans to the Federal Reserve Board for review. Under the final rule, the Federal Reserve Board annually evaluates institutions capital adequacy, internal capital adequacy assessment processes, and their plans to make capital distributions, such as dividend payments or stock repurchases. The Federal Reserve Board will approve dividend increases or other capital distributions only for companies whose capital plans receive a non-objection by supervisors and are able to demonstrate sufficient financial strength to operate as successful financial intermediaries under stressed macroeconomic and financial market scenarios, after making the desired capital distributions. The Federal Reserve Board annually issues instructions outlining the information it is seeking from the covered firms, including the Corporation, and the evaluation the Federal Reserve Board will do of the capital plans. The level of detail and analysis expected in each institution s capital plan varies based on the company s size, complexity, risk profile, and scope of operations. In January 2012, the Corporation submitted its first capital plan to the Federal Reserve Board, and its second capital plan was submitted on January 7, 2013.

Capital Adequacy Requirements

The regulators view capital levels as important indicators of an institution s financial soundness. As a general matter, FDIC-insured depository institutions and their holding companies (including the Bank and the Corporation) are required to maintain minimum capital relative to the amount and types of assets they hold. The final supervisory determination on an institution s capital adequacy is based on the regulator s assessment of numerous factors.

The Federal Reserve Board has established risk-based and leverage capital guidelines for bank holding companies, including the Corporation. The current risk-based capital guidelines that apply to the Corporation and the Bank, commonly referred to as Basel I, are based upon the 1988 capital accord of the International Basel Committee on Banking Supervision (Basel Committee), a committee of central banks and bank supervisors, as implemented by the Federal Reserve Board. As discussed further below, the federal bank regulatory agencies have adopted new risk-based capital guidelines for core banks, including the Corporation, based upon the Revised Framework for the International Convergence of Capital Measurement and Capital Standards (Basel II) issued by the Basel Committee in November 2005.

Basel I

Under the existing Basel I-based guidelines, the minimum ratio of total capital to risk-weighted assets (which are primarily the credit risk equivalents of balance sheet assets and certain off-balance sheet items such as standby letters of credit, but also include a nominal market risk equivalent balance related to foreign exchange and debt/equity trading activities) is eight percent. At least half of the total capital must be composed of tier 1 capital, which includes common stockholders equity (including retained earnings), qualifying non-cumulative perpetual preferred stock (and, for bank holding companies only, a limited amount of qualifying cumulative perpetual preferred stock and a limited amount of trust preferred securities), and minority interests in the equity accounts of consolidated subsidiaries, less goodwill, other disallowed intangibles, and disallowed deferred tax assets, among other items. The Federal Reserve Board also has adopted a minimum leverage ratio for bank holding companies, requiring tier 1 capital of at least three percent of average quarterly total consolidated assets (as defined for regulatory purposes), net of goodwill and certain other intangible assets.

The federal banking regulators have also established risk-based and leverage capital guidelines that FDIC- insured depository institutions are required to meet. These regulations are generally similar to those established by the Federal Reserve Board for bank holding companies. The risk-based and leverage capital ratios for the Corporation and the Bank, together with the regulatory minimum ratios and the ratios required for classification as well-capitalized, are provided in the following chart.

	Risk-Based and Leverage Ratios as of December 31, 2012		
	Tier 1 Capital	Total Capital	Leverage Ratio
Northern Trust Corporation	12.8%	14.3%	8.2%
The Northern Trust Company	11.9	13.7	7.6
Minimum required ratio	4.0	8.0	3.0
Well capitalized minimum ratio	6.0	10.0	5.0

Basel II

As mentioned above, the Corporation also is subject to the Basel II framework for risk-based capital adequacy. The U.S. bank regulatory agencies have issued final rules with respect to implementation of the Basel II framework. Under the final Basel II rules, the Corporation is one of a small number of core banking organizations. As a result, the Corporation and the Bank will be required to use the advanced approaches under Basel II for calculating risk-based capital related to credit risk and operational risk, instead of the methodology reflected in the regulations effective prior to adoption of Basel II. The rules also require core banking organizations to have rigorous processes for assessing overall capital adequacy in relation to their total risk profiles, and to publicly disclose certain information about their risk profiles and capital adequacy.

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The Corporation has for several years been preparing to comply with the advanced approaches of the Basel II framework. In order to implement the rules, a core banking organization, such as the Corporation, was required to adopt (and the Corporation did adopt) an implementation plan and satisfactorily complete a parallel run, in which it calculated capital requirements under both the Basel II rules and regulations effective prior to the adoption of Basel II. In the U.S., the Corporation entered the parallel run in April 2010.

The Corporation is also addressing issues related to implementation timing differences between the U.S. and other jurisdictions, to ensure that the Corporation and its depository institution subsidiaries comply with regulatory requirements and expectations in all jurisdictions where they operate. The Corporation s U.K., Guernsey and Canadian entities subject to Basel II rules have already adopted the standardized approach for credit risk and the basic indicator approach for operational risk in calculating minimum regulatory capital requirements.

Basel III

On December 16, 2010, the Basel Committee released its final framework for strengthening international capital and liquidity regulation, known as Basel III. The Basel III calibration and phase-in arrangements were previously endorsed by the Seoul G20 Leaders Summit in November 2010, and will be subject to individual adoption by member nations, including the U.S. Under these standards, when fully phased-in on January 1, 2019, banking institutions will be required to satisfy three risk-based capital ratios:

A common equity tier 1 ratio of at least 7.0%, inclusive of 4.5% minimum common equity tier 1 ratio, net of regulatory deductions, and the new 2.5% capital conservation buffer of common equity to risk-weighted assets;

A tier 1 capital ratio of at least 8.5%, inclusive of the 2.5% capital conservation buffer; and

A total capital ratio of at least 10.5%, inclusive of the 2.5% capital conservation buffer.

The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a common equity tier 1 ratio above the minimum but below the conservation buffer may face constraints on dividends, equity repurchases, and compensation based on the amount of such shortfall. The Basel Committee also announced that a countercyclical buffer of 0% to 2.5% of common equity or other loss-absorbing capital will be implemented according to national circumstances as an extension of the conservation buffer during periods of excess credit growth.

Basel I and Basel II do not include a leverage requirement as an international standard. However, Basel III introduces a non-risk adjusted tier 1 leverage ratio of 3%, based on a measure of total exposure rather than total assets and new liquidity standards.

The Basel Committee had initially planned for member nations to begin implementing the Basel III requirements by January 1, 2013, with full implementation by January 1, 2019. On November 9, 2012, U.S. regulators announced that implementation of Basel III s first requirements would be delayed until an undetermined future date. The regulators made no indication that any other future regulatory phase-in dates would be delayed.

On November 4, 2011 the Basel Committee issued its final rule setting forth proposals to apply a new common equity tier 1 surcharge to certain designated global systemically important banks (GSIBs). GSIBs subject to the surcharge are identified by application of a quantitative indicator-based approach for evaluating systemic risk that weights both categories and indicators of size, substitutability, interconnectedness, cross-jurisdictional activity, and complexity. On November 1, 2012, using the Basel Committee s methodology, the Financial Stability Board (FSB) and the Basel Committee identified 28 financial institutions determined to be GSIBs. The group of GSIBs is updated annually and published by the FSB each November. At this time, the Corporation has not been designated as a GSIB. The GSIBs equity surcharge provisions, like the rest of Basel III, are subject to interpretation and implementation by U.S. regulatory authorities.

Under the Dodd-Frank Act, for SIFIs, including the Corporation, the Federal Reserve Board may increase the capital buffer. The purpose of these new capital requirements is to ensure financial institutions are better capitalized to withstand periods of unfavorable financial and economic conditions. The Dodd-Frank Act also requires the establishment of more stringent prudential standards by requiring the federal banking agencies to adopt capital and liquidity requirements which address the risks that the activities of an institution pose to the institution and the public and private stakeholders, including risks arising from certain enumerated activities. In particular, the Dodd-Frank Act excludes trust preferred securities issued on or after May 19, 2010 from tier 1 capital. For depository institution holding companies with total consolidated assets of more than $15 billion at December 31, 2009, trust preferred securities issued before May 19, 2010 will be phased-out of tier 1 capital over a three-year period.

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On June 7, 2012 the Board of Governors of the Federal Reserve, in conjunction with the Office of the Comptroller of the Currency and the FDIC, published three notices of proposed rulemaking related to Basel III. The proposed rules include two calculation methods: a standardized approach, applicable to all depository institutions, bank holding companies with consolidated assets of $500 million or more, and savings and loan holding companies, and an advanced approach, generally applicable only to the largest, most internationally active banking organizations. The Corporation and Bank will calculate their capital ratios under both the standardized and advanced approaches. Under the proposed rules, the Corporation and the Bank must maintain capital levels that exceed the adequately capitalized minimum ratios under the most constraining of the two approaches. For advanced approaches institutions, the proposed rules state that for the capital conservation buffer, any countercyclical capital buffer applied, and any other capital surcharges that are applied, a depository institution s or bank holding company s capital adequacy will be assessed using the advanced approaches.

The ultimate impact of the new capital and liquidity standards on the Corporation and the Bank is currently being reviewed and will depend on a number of factors, including the rulemaking and implementation by the U.S. banking regulators. The Corporation cannot determine the ultimate effect that potential legislation, or subsequent regulations, if enacted, would have upon the Corporation s earnings or financial position. In addition, significant questions remain as to how the capital and liquidity mandates of the Dodd-Frank Act will be integrated with the requirements of Basel III. However, as the Corporation currently understands Basel III, it believes its capital strength, balance sheet and business model leave it well positioned for Basel III.

Prompt Corrective Action

Under the FDIA, the federal banking agencies must take prompt corrective action against undercapitalized U.S. depository institutions. U.S. depository institutions are assigned one of five capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, and are subjected to differential regulation corresponding to the capital category within which the institution falls. A depository institution is deemed to be well capitalized if the banking institution has a total risk-based capital ratio of 10.0% or greater, a tier 1 risk-based capital ratio of 6.0% or greater, and a leverage ratio of 5.0% or greater, and the institution is not subject to an order, written agreement, capital directive, or prompt corrective action directive to meet and maintain a specific level for any capital measure. Under certain circumstances, a well capitalized, adequately capitalized or undercapitalized institution may be treated as if the institution were in the next lower capital category. A banking institution that is undercapitalized is required to submit a capital restoration plan. Failure to meet capital guidelines could subject the Bank to a variety of enforcement remedies by federal bank regulatory agencies, including: termination of deposit insurance by the FDIC, restrictions on certain business activities, and appointment of the FDIC as conservator or receiver. As of December 31, 2012, the Corporation and the Bank exceeded the required capital ratios for classification as well capitalized.

Examination and Enforcement Powers of the Federal Banking Agencies

A principal objective of the U.S. bank regulatory system is to protect depositors by ensuring the financial safety and soundness of banks. To that end, the banking regulators have broad regulatory, examination, and enforcement powers, including the power to issue cease and desist orders, impose substantial fines and other civil and criminal penalties, terminate deposit insurance and appoint a conservator or receiver. Failure to comply with applicable laws, regulations, and supervisory agreements could subject the Corporation and its banking subsidiaries, as well as officers, directors, and other institution-affiliated parties of these organizations, to administrative sanctions and potentially substantial civil money penalties. The appropriate federal banking agency may appoint the FDIC as conservator or receiver for a banking institution (or the FDIC may appoint itself, under certain circumstances) if any one or more of a number of circumstances exist, including, without limitation, the fact that the banking institution:

is undercapitalized and has no reasonable prospect of becoming adequately capitalized;

fails to become adequately capitalized when required to do so;

fails to submit a timely and acceptable capital restoration plan;

materially fails to implement an accepted capital restoration plan; or fails to submit an acceptable resolution plan.

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The FDIC may terminate a depository institution s deposit insurance upon a finding that the institution s financial condition is unsafe or unsound or that the institution has engaged in unsafe or unsound practices or has violated any applicable rule, regulation, order or condition enacted or imposed by the institution s regulatory agency. Engaging in unsafe or unsound practices or failing to comply with applicable laws, regulations and supervisory agreements could subject the Bank, the Corporation, and other subsidiaries of the Corporation, or their officers, directors, and institution-affiliated parties to the remedies described above and other sanctions.

Restrictions on Transactions with Affiliates and Insiders

FDIC-insured banks, including the Corporation s bank subsidiaries, are subject to restrictions under Sections 23A and 23B of the Federal Reserve Act (as implemented by Regulation W), which govern transactions between FDIC-insured banks and any affiliated entity, whether that entity is the bank s parent holding company, a holding company affiliate of the bank or a subsidiary of the bank. Regulation W restrictions apply to certain covered transactions, including extensions of credit, issuance of guarantees, investments or asset purchases. In general, these restrictions require that any extensions of credit must be fully secured with qualifying collateral and are limited, as to any one of the Corporation or such non-bank affiliates, to 10% of the lending bank s capital stock and surplus, and, as to the Corporation and all such non-bank affiliates in the aggregate, to 20% of such lending bank s capital stock and surplus. These restrictions, other than the 10% of capital limit on covered transactions with any one affiliate, are also applied to transactions between banks and their financial subsidiaries. Furthermore, these transactions must be on terms and conditions that are, or in good faith would be, offered to nonaffiliated companies (i.e., at arm s length).

The Dodd-Frank Act generally enhances the restrictions on transactions with affiliates under Sections 23A and 23B of the Federal Reserve Act, including an expansion of the definition of covered transactions to include credit exposures related to derivatives, repurchase agreements and securities lending arrangements, and an increase in the amount of time for which collateral requirements regarding covered credit transactions must be satisfied. The definition of affiliate was expanded to include any investment fund to which the Corporation or an affiliate serves as an investment adviser. The ability of the Federal Reserve Board to grant exemptions from these restrictions was also narrowed, including by requiring coordination with other bank regulators. In addition, the provision in Section 23A that permits a bank to engage in covered transactions with a financial subsidiary of the bank in an amount greater than 10% (but less than 20%) of the bank s capital and surplus has been eliminated.

The restrictions on loans to directors, executive officers, principal stockholders and their related interests (collectively referred to herein as insiders) contained in the Federal Reserve Act and Regulation O apply to all federally insured institutions. These restrictions include limits on loans to one borrower and conditions that must be met before such a loan can be made. There is also an aggregate limitation on all loans (including credit exposures related to derivatives, repurchase agreements and securities lending arrangements) to insiders and their related interests. These loans cannot exceed the institution s total unimpaired capital and surplus, and the FDIC may determine that a lesser amount is appropriate. Insiders are subject to enforcement actions for knowingly accepting loans in violation of applicable restrictions. The Dodd-Frank Act enhanced these restrictions and also imposed restrictions on the purchase or sale of assets between banking institutions and insiders.

Anti-Money Laundering, Anti-Terrorism Legislation, and Office of Foreign Assets Control

Under federal law, including the Bank Secrecy Act, the USA PATRIOT Act, and the International Money Laundering Abatement and Anti-Terrorist Financing Act, financial institutions (including insured depository institutions, broker-dealers and certain other financial institutions) must maintain anti-money laundering programs that include established internal policies, procedures, and controls; a designated compliance officer; an ongoing employee training program; and testing of the program by an independent audit function. Financial institutions are prohibited from entering into specified financial transactions and account relationships and must meet enhanced standards for due diligence and client identification in their dealings with non-U.S. financial institutions and non-U.S. clients. Financial institutions must take reasonable steps to conduct enhanced scrutiny of account relationships to guard against money laundering and to report any suspicious transactions, and law enforcement authorities have been granted increased access to financial information maintained by financial institutions. Bank regulators routinely examine institutions for compliance with these obligations and they must consider an institution s compliance in connection with the regulatory review of applications, including applications for banking mergers and acquisitions. The regulatory authorities have imposed cease and desist orders and civil money penalty sanctions against institutions found to be violating these obligations.

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The U.S. Department of the Treasury s Office of Foreign Assets Control (OFAC) is responsible for requiring that U.S. entities do not engage in transactions with certain prohibited parties, as defined by various Executive Orders and Acts of Congress. OFAC publishes lists of persons, organizations and countries suspected of aiding, harboring or engaging in terrorist acts, known as Specially Designated Nationals and Blocked Persons. If the Corporation or the Bank finds a name on any transaction, account or wire transfer that is on an OFAC list, the Corporation or the Bank must freeze or block such account or transaction, file a suspicious activity report and notify the appropriate authorities.

Many other countries have imposed similar laws and regulations that apply to the Corporation s non-U.S. offices. The Corporation has established policies and procedures to comply with these laws and the related regulations in all relevant jurisdictions. Additionally, neither the Company nor any of its affiliates or subsidiaries have engaged in activities which are sanctionable under the Iran Sanctions Act or the Comprehensive Iran Sanctions, Accountability, and Divestment Act (CISADA); engaged in transactions with the government Iran or persons whose assets are frozen pursuant to executive orders dealing with terrorism or weapons of mass destruction proliferation; or engaged in the transfer of goods, technology, or services to Iran that are likely to be used for human rights abuses against the Iranian people.

Deposit Insurance and Assessments

FDIC-insured depository institutions are required to pay deposit insurance assessments to the FDIC. The amount of a particular institution s deposit insurance assessment is based on that institution s risk classification under an FDIC risk-based assessment system. An institution s risk classification is assigned based on the level of supervisory concern the institution poses to the regulators, the institution s capital levels and other risk measures.

The Dodd-Frank Act makes permanent the general $250,000 deposit insurance limit for insured deposits. Federal deposit insurance for the full net amount of deposits in noninterest bearing transaction accounts expired on December 31, 2012 for all insured banks.

The Dodd-Frank Act increased the minimum designated reserve ratio of the DIF from 1.15% to 1.35% of the estimated amount of total insured deposits effective September 30, 2020, eliminated the upper limit for the reserve ratio designated by the FDIC each year, and eliminated the requirement that the FDIC pay dividends to depository institutions when the reserve ratio exceeds certain thresholds. On December 14, 2010, the FDIC raised the minimum designated reserve ratio of the DIF to 2%, where it remains today. The ratio is higher than the minimum reserve ratio of 1.35% as set by the Dodd-Frank Act.

The FDIC s rule on Assessments, Dividends, Assessment Base and Large Bank Pricing, mandated by the Dodd-Frank Act, changes the deposit insurance assessment system from one that is based on domestic deposits to one that is based on average consolidated total assets minus average tangible equity. Because the new assessment base under the Dodd-Frank Act is larger than the old assessment base, the final rule s assessment rates are lower than the older rates, which achieves the FDIC s goal of not significantly altering the total amount of revenue collected from the industry. In addition, the rule adopts a scorecard assessment scheme for larger banks and suspends dividend payments if the DIF reserve ratio exceeds 1.5% but provides for decreasing assessment rates when the DIF reserve ratio reaches certain thresholds. The rule further reduces the assessment base for custodial banks by the daily or weekly average of a certain amount of low-risk assets (i.e., assets with a Basel risk weighting of 0%, regardless of maturity, plus 50% of assets with a Basel risk weighting of 20%, again regardless of maturity) subject to the limitation that the daily or weekly average value of these assets cannot exceed the daily or weekly average value of those deposits classified as transaction accounts and identified by the institution as being directly linked to a fiduciary or custodial and safekeeping account. The rule identifies custodial banks as insured depository institutions with previous calendar year-end trust assets (i.e., fiduciary and custody and safekeeping assets) of at least $50 billion or those insured depository institutions that derived more than 50% of their revenue (interest income plus non-interest income) from trust activity over the previous calendar year. Under the final rule, the Bank will pay slightly lower assessments to the DIF than under the old system.

Continued action by the FDIC to replenish the DIF as well as the changes contained in the Dodd-Frank Act may result in higher assessment rates, which could reduce the profitability of or otherwise negatively impact the Bank.

Interstate Banking and Branching

The Dodd-Frank Act amends the BHCA to require a bank holding company seeking approval to acquire shares of a bank located outside of the bank holding company s home state to be well-capitalized and well-managed. Similarly, the Dodd-Frank Act amends the Bank Merger Act to require that the surviving bank in an interstate merger transaction be well-capitalized and well-managed.

In addition, national banks and state banks with different home states are permitted to merge across state lines, with the approval of the appropriate federal banking agency, unless the home state of a participating banking institution passed legislation prior to June 1, 1997 that expressly prohibits interstate mergers. The Dodd-Frank Act permits a national bank or a state bank, with the approval of its regulator, to open a branch in any state if the law of the state in which the branch is to be located would permit the establishment of the branch if the bank were a bank chartered in that state.

Community Reinvestment Act

The Corporation s banking subsidiaries are subject to the CRA. The CRA and the regulations issued thereunder are intended to encourage banks to help meet the credit needs of their service areas, including low and moderate income neighborhoods, consistent with the safe and sound operations of the banks. These regulations also provide for regulatory assessment of a bank s record in meeting the needs of its service area when considering applications to establish branches, merger applications, and applications to acquire the assets and assume the liabilities of another bank. Federal banking agencies are required to make public the rating of a bank s performance under the CRA. In the case of a bank holding company, the CRA performance record of its bank subsidiaries is reviewed by federal banking agencies in connection with the filing of an application to acquire ownership or control of shares or assets of a bank or thrift or to merge with any other bank holding company. An unsatisfactory record can substantially delay or block the transaction. The Bank in its most recent CRA examination received an outstanding CRA rating from its regulator.

In addition, federal law requires the disclosure of agreements reached with community groups that relate