Introduction

The Goldman Sachs Group, Inc. (Group Inc.) is a leading global investment banking, securities and investment management firm that provides a wide range of financial services to a substantial and diversified client base that includes corporations, financial institutions, governments and high-net-worth individuals. Founded in 1869, the firm is headquartered in New York and maintains offices in all major financial centers around the world.

We report our activities in four business segments: Investment Banking, Institutional Client Services, Investing & Lending and Investment Management. See "Results of Operations" below for further information about our business segments.

When we use the terms "Goldman Sachs," "the firm," "we," "us" and "our," we mean Group Inc., a Delaware corporation, and its consolidated subsidiaries.

References herein to our Annual Report on Form 10-K are to our Annual Report on Form 10-K for the year ended December 31, 2012. All references to 2012, 2011 and 2010 refer to our years ended, or the dates, as the context requires, December 31, 2012, December 31, 2011 and December 31, 2010, respectively. Any reference to a future year refers to a year ending on December 31 of that year. Certain reclassifications have been made to previously reported amounts to conform to the current presentation.

In this discussion and analysis of our financial condition and results of operations, we have included information that may constitute "forward-looking statements" within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements are not historical facts, but instead represent only our beliefs regarding future events, many of which, by their nature, are inherently uncertain and outside our control. This information includes statements other than historical information or statements of current condition and may relate to our future plans and objectives and results, among other things, and may also include statements about the objectives and effectiveness of our risk management and liquidity policies, statements about trends in or growth opportunities for our businesses, statements about our future status, activities or reporting under U.S. or non-U.S. banking and financial regulation, and statements about our investment banking transaction backlog. By identifying these statements for you in this manner, we are alerting you to the possibility that our actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these forward-looking statements. Important factors that could cause our actual results and financial condition to differ from those indicated in these forward-looking statements include, among others, those discussed below under "Certain Risk Factors That May Affect Our Businesses" as well as "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K and "Cautionary Statement Pursuant to the U.S. Private Securities Litigation Reform Act of 1995" in Part I, Item 1 of our Annual Report on Form 10-K.

Executive Overview

The firm generated net earnings of $7.48 billion for 2012, compared with $4.44 billion and $8.35 billion for 2011 and 2010, respectively. Our diluted earnings per common share were $14.13 for 2012, compared with $4.51 [1] for 2011 and $13.18 [2] for 2010. Return on average common shareholders' equity (ROE) [3] was 10.7% for 2012, compared with 3.7% [1] for 2011 and 11.5% [2] for 2010.

Book value per common share increased approximately 11% to $144.67 and tangible book value per common share [4] increased approximately 12% to $134.06 compared with the end of 2011. During the year, the firm repurchased 42.0 million shares of its common stock for a total cost of $4.64 billion. Our Tier 1 capital ratio under Basel 1 was 16.7% and our Tier 1 common ratio under Basel 1 [5] was 14.5% as of December 2012.

The firm generated net revenues of $34.16 billion for 2012. These results reflected significantly higher net revenues in Investing & Lending, as well as higher net revenues in Institutional Client Services, Investment Banking and Investment Management compared with 2011.

An overview of net revenues for each of our business segments is provided below.

Investment Banking

Net revenues in Investment Banking increased compared with 2011, reflecting significantly higher net revenues in our Underwriting business, due to strong net revenues in debt underwriting. Net revenues in debt underwriting were significantly higher compared with 2011, primarily reflecting higher net revenues from investment-grade and leveraged finance activity. Net revenues in equity underwriting were lower compared with 2011, primarily reflecting a decline in industry-wide initial public offerings. Net revenues in Financial Advisory were essentially unchanged compared with 2011.

Institutional Client Services

Net revenues in Institutional Client Services increased compared with 2011, reflecting higher net revenues in Fixed Income, Currency and Commodities Client Execution.

The increase in Fixed Income, Currency and Commodities Client Execution compared with 2011 reflected strong net revenues in mortgages, which were significantly higher compared with 2011. In addition, net revenues in credit products and interest rate products were solid and higher compared with 2011. These increases were partially offset by significantly lower net revenues in commodities and slightly lower net revenues in currencies. Although broad market concerns persisted during 2012, Fixed Income, Currency and Commodities Client Execution operated in a generally improved environment characterized by tighter credit spreads and less challenging market-making conditions compared with 2011.

1. Excluding the impact of the preferred dividend of $1.64 billion in the first quarter of 2011 (calculated as the difference between the carrying value and the redemption value of the preferred stock), related to the redemption of our 10% Cumulative Perpetual Preferred Stock, Series G (Series G Preferred Stock) held by Berkshire Hathaway Inc. and certain of its subsidiaries (collectively, Berkshire Hathaway), diluted earnings per common share were $7.46 and ROE was 5.9% for 2011. We believe that presenting our results for 2011 excluding this dividend is meaningful, as it increases the comparability of period-to-period results. Diluted earnings per common share and ROE excluding this dividend are non-GAAP measures and may not be comparable to similar non-GAAP measures used by other companies. See "Results of Operations — Financial Overview" below for further information about our calculation of diluted earnings per common share and ROE excluding the impact of this dividend.

2. Excluding the impact of the $465 million related to the U.K. bank payroll tax, the $550 million related to the SEC settlement and the $305 million impairment of our New York Stock Exchange (NYSE) Designated Market Maker (DMM) rights, diluted earnings per common share were $15.22 and ROE was 13.1% for 2010. We believe that presenting our results for 2010 excluding the impact of these items is meaningful, as it increases the comparability of period-to-period results. Diluted earnings per common share and ROE excluding these items are non-GAAP measures and may not be comparable to similar non-GAAP measures used by other companies. See "Results of Operations — Financial Overview" below for further information about our calculation of diluted earnings per common share and ROE excluding the impact of these items.

3. See "Results of Operations — Financial Overview" below for further information about our calculation of ROE.

4. Tangible book value per common share is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies. See "Equity Capital — Other Capital Metrics" below for further information about our calculation of tangible book value per common share.

5. Tier 1 common ratio is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies. See "Equity Capital — Consolidated Regulatory Capital Ratios" below for further information about our Tier 1 common ratio.

Net revenues in Equities were essentially unchanged compared with 2011. Net revenues in securities services were significantly higher compared with 2011, reflecting a gain of approximately $500 million on the sale of our hedge fund administration business. In addition, equities client execution net revenues were higher than 2011, primarily reflecting significantly higher results in cash products, principally due to increased levels of client activity. These increases were offset by lower commissions and fees, reflecting lower market volumes. During 2012, Equities operated in an environment generally characterized by an increase in global equity prices and lower volatility levels.

The net loss attributable to the impact of changes in our own credit spreads on borrowings for which the fair value option was elected was $714 million ($433 million and $281 million related to Fixed Income, Currency and Commodities Client Execution and equities client execution, respectively) for 2012, compared with a net gain of $596 million ($399 million and $197 million related to Fixed Income, Currency and Commodities Client Execution and equities client execution, respectively) for 2011.

Investing & Lending

Net revenues in Investing & Lending were $5.89 billion and $2.14 billion for 2012 and 2011, respectively. During 2012, Investing & Lending net revenues were positively impacted by tighter credit spreads and an increase in global equity prices. Results for 2012 included a gain of $408 million from our investment in the ordinary shares of Industrial and Commercial Bank of China Limited (ICBC), net gains of $2.39 billion from other investments in equities, primarily in private equities, net gains and net interest income of $1.85 billion from debt securities and loans, and other net revenues of $1.24 billion, principally related to our consolidated investment entities.

Results for 2011 included a loss of $517 million from our investment in the ordinary shares of ICBC and net gains of $1.12 billion from other investments in equities, primarily in private equities, partially offset by losses from public equities. In addition, Investing & Lending included net revenues of $96 million from debt securities and loans. This amount includes approximately $1 billion of unrealized losses related to relationship lending activities, including the effect of hedges, offset by net interest income and net gains from other debt securities and loans. Results for 2011 also included other net revenues of $1.44 billion, principally related to our consolidated investment entities.

Investment Management

Net revenues in Investment Management increased compared with 2011, due to significantly higher incentive fees, partially offset by lower transaction revenues and slightly lower management and other fees. During the year, assets under supervision [1] increased $70 billion to $965 billion. Assets under management increased $26 billion to $854 billion, reflecting net market appreciation of $44 billion, primarily in fixed income and equity assets, partially offset by net outflows of $18 billion. Net outflows in assets under management included outflows in equity, alternative investment and money market assets, partially offset by inflows in fixed income assets [2]. Other client assets increased $44 billion to $111 billion, primarily due to net inflows [2], principally in client assets invested with third-party managers and assets related to advisory relationships.

Our businesses, by their nature, do not produce predictable earnings. Our results in any given period can be materially affected by conditions in global financial markets, economic conditions generally and other factors. For a further discussion of the factors that may affect our future operating results, see "Certain Risk Factors That May Affect Our Businesses" below, as well as "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K.

1. Assets under supervision include assets under management and other client assets. Assets under management include client assets where we earn a fee for managing assets on a discretionary basis. Other client assets include client assets invested with third-party managers, private bank deposits and assets related to advisory relationships where we earn a fee for advisory and other services, but do not have discretion over the assets.

2. Includes $34 billion of fixed income asset inflows in connection with our acquisition of Dwight Asset Management Company LLC (Dwight Asset Management), including $17 billion in assets under management and $17 billion in other client assets, and $5 billion of fixed income and equity asset outflows in connection with our liquidation of Goldman Sachs Asset Management Korea Co., Ltd. (Goldman Sachs Asset Management Korea, formerly known as Macquarie — IMM Investment Management), all related to assets under management, for the year ended December 2012.

Business Environment

Global economic conditions generally weakened in 2012, as real gross domestic product (GDP) growth slowed in most major economies. Market sentiment was affected by continued broad market concerns and uncertainties, although positive developments helped to improve market conditions. These developments included certain central bank actions to ease monetary policy and address funding risks for European financial institutions. In addition, the U.S. economy posted stable to improving economic data, including favorable developments in unemployment and housing. These improvements resulted in tighter credit spreads, higher global equity prices and lower levels of volatility. However, concerns about the outlook for the global economy and continued political uncertainty, particularly the political debate in the United States surrounding the fiscal cliff, generally resulted in client risk aversion and lower activity levels. Also, uncertainty over financial regulatory reform persisted. These concerns weighed on investment banking activity, as completed mergers and acquisitions activity declined compared with 2011, and equity and equity-related underwriting activity remained low, particularly in initial public offerings. However, industry-wide debt underwriting activity improved compared with 2011. For a further discussion of how market conditions may affect our businesses, see "Certain Risk Factors That May Affect Our Businesses" below as well as "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K.

Global

During 2012, real GDP growth declined in most advanced economies and emerging markets. In advanced economies, the slowdown primarily reflected a decline in consumer expenditure and fixed investment growth, particularly in Europe, as well as a deceleration in international trade compared with 2011. In emerging markets, growth in domestic demand weakened, although the contribution from government spending was generally positive. Unemployment levels declined slightly in some economies compared with 2011, but increased in others, particularly in the Euro area. The rate of unemployment continued to remain elevated in many advanced economies. During 2012, the U.S. Federal Reserve, the Bank of England and the Bank of Japan left interest rates unchanged, while the European Central Bank reduced its interest rate. In addition, the People's Bank of China lowered its one-year benchmark lending rate during the year. The price of crude oil generally declined during 2012. The U.S. dollar weakened against both the Euro and the British pound, while it strengthened against the Japanese yen.

United States

In the United States, real GDP increased by 2.2% in 2012, compared with an increase of 1.8% in 2011. Growth was supported by an acceleration in residential investment and a smaller decrease in state and local government spending, which were partially offset by a slowdown in consumer spending and business investment. Both house prices and housing starts increased. Industrial production expanded in 2012, despite the negative impact of Hurricane Sandy during the fourth quarter. Business and consumer confidence declined during parts of the year, primarily reflecting increased global economic concerns and heightened uncertainties, but ended the year higher compared with the end of 2011. Measures of core inflation on average were higher compared with 2011. The unemployment rate declined during 2012, but remained elevated. The U.S. Federal Reserve maintained its federal funds rate at a target range of zero to 0.25% during the year and extended its program to lengthen the maturity of the U.S. Treasury debt it holds. In addition, the U.S. Federal Reserve announced an open-ended program to purchase U.S. Treasury securities and mortgage-backed securities, as well as a commitment to keep short-term interest rates exceptionally low until the unemployment rate falls to 6.5% or inflation rises materially. The yield on the 10-year U.S. Treasury note fell by 11 basis points during 2012 to 1.78%. In equity markets, the NASDAQ Composite Index, the S&P 500 Index and the Dow Jones Industrial Average increased by 16%, 13% and 7%, respectively, compared with the end of 2011.

Europe

In the Euro area, real GDP declined by 0.5% in 2012, compared with an increase of 1.5% in 2011. The contraction was principally due to a sharp fall in domestic demand, primarily reflecting downturns in consumer spending and fixed investment. Business and consumer confidence declined and measures of core inflation increased slightly during the year. The unemployment rate increased substantially, particularly in Spain and Italy. These negative developments reflected the impact that the sovereign debt crisis had on the region's economic growth, particularly during the first half of the year, as concerns about Greece's debt situation and the fiscal outlook in Spain and Italy intensified. To address these issues, the European Central Bank injected liquidity in the Eurosystem through its longer-term refinancing operations (LTROs), decreased its main refinancing operations rate by 25 basis points to 0.75%, and announced a program to make outright purchases of sovereign bonds in the secondary markets. The Euro appreciated by 2% against the U.S. dollar. In the United Kingdom, real GDP increased by 0.2% in 2012 compared with an increase of 0.9% in 2011. The Bank of England maintained its official bank rate at 0.50% and increased the size of its asset purchase program. The British pound appreciated by 4% against the U.S. dollar. Long-term government bond yields generally declined during the year. In equity markets, the DAX Index, the CAC 40 Index, the Euro Stoxx 50 Index, and the FTSE 100 Index increased by 29%, 15%, 14% and 6%, respectively, compared with the end of 2011.

Asia

In Japan, real GDP increased by 1.9% in 2012, compared with a decline of 0.6% in 2011. Fixed investment growth increased, particularly from the public sector, helped by reconstruction efforts following the earthquake and tsunami in 2011. However, the trade balance continued to deteriorate during 2012. Measures of inflation remained negative or close to zero during the year. The Bank of Japan maintained its target overnight call rate at a range of zero to 0.10% during the year, increased the size of its asset purchase program, and announced measures to facilitate outright purchases of government and corporate bonds. The yield on 10-year Japanese government bonds fell by 20 basis points during the year to 0.79%. The Japanese yen depreciated by 13% against the U.S. dollar and, in equity markets, the Nikkei 225 Index increased by 23%. In China, real GDP increased by 7.8% in 2012, compared with an increase of 9.3% in 2011. Growth slowed as household consumption and fixed investment growth moderated. In addition, growth in industrial production declined. Measures of inflation declined during the year. The People's Bank of China lowered its one-year benchmark lending rate by 56 basis points to 6.00% and reduced the reserve requirement ratio by 100 basis points during the year. The Chinese yuan appreciated slightly against the U.S. dollar and, in equity markets, the Shanghai Composite Index increased by 3%. In India, real GDP increased by an estimated 5.4% in 2012, compared with an increase of 7.5% in 2011. Growth decelerated, primarily reflecting a slowdown in domestic demand growth and a deterioration in the trade balance. The rate of wholesale inflation declined compared with 2011, but remained elevated. The Indian rupee depreciated by 4% against the U.S. dollar and, in equity markets, the BSE Sensex Index increased 26%. Equity markets in Hong Kong and South Korea were higher, as the Hang Seng Index increased 23% and the KOSPI Composite Index increased 9%, respectively, compared with the end of 2011.

Other Markets

In Brazil, real GDP increased by an estimated 1.0% in 2012, compared with an increase of 2.7% in 2011. Growth decelerated, primarily reflecting a decline in private consumption growth and a downturn in fixed investment. The Brazilian real depreciated by 9% against the U.S. dollar and, in equity markets, the Bovespa Index increased by 7% compared with the end of 2011. In Russia, real GDP increased by 3.4% in 2012, compared with 4.3% in 2011. Growth slowed, primarily reflecting a decline in domestic demand growth, particularly during the second half of the year. The Russian ruble appreciated by 5% against the U.S. dollar and, in equity markets, the MICEX Index increased by 5% compared with the end of 2011.

Critical Accounting Policies

Fair Value

Fair Value Hierarchy. Financial instruments owned, at fair value and Financial instruments sold, but not yet purchased, at fair value (i.e., inventory), as well as certain other financial assets and financial liabilities, are reflected in our consolidated statements of financial condition at fair value (i.e., marked-to-market), with related gains or losses generally recognized in our consolidated statements of earnings. The use of fair value to measure financial instruments is fundamental to our risk management practices and is our most critical accounting policy.

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the hierarchy under U.S. generally accepted accounting principles (U.S. GAAP) gives (i) the highest priority to unadjusted quoted prices in active markets for identical, unrestricted assets or liabilities (level 1 inputs), (ii) the next priority to inputs other than level 1 inputs that are observable, either directly or indirectly (level 2 inputs), and (iii) the lowest priority to inputs that cannot be observed in market activity (level 3 inputs). Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to their fair value measurement.

The fair values for substantially all of our financial assets and financial liabilities are based on observable prices and inputs and are classified in levels 1 and 2 of the fair value hierarchy. Certain level 2 and level 3 financial assets and financial liabilities may require appropriate valuation adjustments that a market participant would require to arrive at fair value for factors such as counterparty and the firm's credit quality, funding risk, transfer restrictions, liquidity and bid/offer spreads. Valuation adjustments are generally based on market evidence.

Instruments categorized within level 3 of the fair value hierarchy are those which require one or more significant inputs that are not observable. As of December 2012 and December 2011, level 3 assets represented 5.0% and 5.2%, respectively, of the firm's total assets. Absent evidence to the contrary, instruments classified within level 3 of the fair value hierarchy are initially valued at transaction price, which is considered to be the best initial estimate of fair value. Subsequent to the transaction date, we use other methodologies to determine fair value, which vary based on the type of instrument. Estimating the fair value of level 3 financial instruments requires judgments to be made. These judgments include:

- determining the appropriate valuation methodology and/or model for each type of level 3 financial instrument;
- determining model inputs based on an evaluation of all relevant empirical market data, including prices evidenced by market transactions, interest rates, credit spreads, volatilities and correlations; and
- determining appropriate valuation adjustments related to illiquidity or counterparty credit quality.

Regardless of the methodology, valuation inputs and assumptions are only changed when corroborated by substantive evidence.

Controls Over Valuation of Financial Instruments. Market makers and investment professionals in our revenue-producing units are responsible for pricing our financial instruments. Our control infrastructure is independent of the revenue-producing units and is fundamental to ensuring that all of our financial instruments are appropriately valued at market-clearing levels. In the event that there is a difference of opinion in situations where estimating the fair value of financial instruments requires judgment (e.g., calibration to market comparables or trade comparison, as described below), the final valuation decision is made by senior managers in control and support functions that are independent of the revenue-producing units (independent control and support functions). This independent price verification is critical to ensuring that our financial instruments are properly valued.

Price Verification. All financial instruments at fair value in levels 1, 2 and 3 of the fair value hierarchy are subject to our independent price verification process. The objective of price verification is to have an informed and independent opinion with regard to the valuation of financial instruments under review. Instruments that have one or more significant inputs which cannot be corroborated by external market data are classified within level 3 of the fair value hierarchy. Price verification strategies utilized by our independent control and support functions include:

- **Trade Comparison.** Analysis of trade data (both internal and external where available) is used to determine the most relevant pricing inputs and valuations.
- **External Price Comparison.** Valuations and prices are compared to pricing data obtained from third parties (e.g., broker or dealers, MarkIt, Bloomberg, IDC, TRACE). Data obtained from various sources is compared to ensure consistency and validity. When broker or dealer quotations or third-party pricing vendors are used for valuation or price verification, greater priority is generally given to executable quotations.
- **Calibration to Market Comparables.** Market-based transactions are used to corroborate the valuation of positions with similar characteristics, risks and components.
- **Relative Value Analyses.** Market-based transactions are analyzed to determine the similarity, measured in terms of risk, liquidity and return, of one instrument relative to another or, for a given instrument, of one maturity relative to another.
- **Collateral Analyses.** Margin disputes on derivatives are examined and investigated to determine the impact, if any, on our valuations.
- **Execution of Trades.** Where appropriate, trading desks are instructed to execute trades in order to provide evidence of market-clearing levels.
- **Backtesting.** Valuations are corroborated by comparison to values realized upon sales.

See Notes 5 through 8 to the consolidated financial statements for further information about fair value measurements.

Review of Net Revenues. Independent control and support functions ensure adherence to our pricing policy through a combination of daily procedures, including the explanation and attribution of net revenues based on the underlying factors. Through this process we independently validate net revenues, identify and resolve potential fair value or trade booking issues on a timely basis and seek to ensure that risks are being properly categorized and quantified.

Review of Valuation Models. The firm's independent model validation group, consisting of quantitative professionals who are separate from model developers, performs an independent model approval process. This process incorporates a review of a diverse set of model and trade parameters across a broad range of values (including extreme and/or improbable conditions) in order to critically evaluate:

- the model's suitability for valuation and risk management of a particular instrument type;
- the model's accuracy in reflecting the characteristics of the related product and its significant risks;
- the suitability of the calculation techniques incorporated in the model;
- the model's consistency with models for similar products; and
- the model's sensitivity to input parameters and assumptions.

New or changed models are reviewed and approved prior to being put into use. Models are evaluated and re-approved annually to assess the impact of any changes in the product or market and any market developments in pricing theories.

Level 3 Financial Assets at Fair Value. The table below presents financial assets measured at fair value and the amount of such assets that are classified within level 3 of the fair value hierarchy.

Total level 3 financial assets were $47.10 billion and $47.94 billion as of December 2012 and December 2011, respectively.

See Notes 5 through 8 to the consolidated financial statements for further information about changes in level 3 financial assets and fair value measurements.

	As of December 2012		As of December 2011	
in millions	Total at Fair Value	Level 3 Total	Total at Fair Value	Level 3 Total
Commercial paper, certificates of deposit, time deposits and other money market instruments	$ 6,057	$ —	$ 13,440	$ —
U.S. government and federal agency obligations	93,241	—	87,040	—
Non-U.S. government and agency obligations	62,250	26	49,205	148
Mortgage and other asset-backed loans and securities:				
Loans and securities backed by commercial real estate	9,805	3,389	6,699	3,346
Loans and securities backed by residential real estate	8,216	1,619	7,592	1,709
Bank loans and bridge loans	22,407	11,235	19,745	11,285
Corporate debt securities	20,981	2,821	22,131	2,480
State and municipal obligations	2,477	619	3,089	599
Other debt obligations	2,251	1,185	4,362	1,451
Equities and convertible debentures	96,454	14,855	65,113	13,667
Commodities	11,696	—	5,762	—
Total cash instruments	335,835	35,749	284,178	34,685
Derivatives	71,176	9,920	80,028	11,900
Financial instruments owned, at fair value	407,011	45,669	364,206	46,585
Securities segregated for regulatory and other purposes	30,484	—	42,014	—
Securities purchased under agreements to resell	141,331	278	187,789	557
Securities borrowed	38,395	—	47,621	—
Receivables from customers and counterparties	7,866	641	9,682	795
Other assets [1]	13,426	507	—	—
Total	$638,513	$47,095	$651,312	$47,937

1. Consists of assets classified as held for sale related to our reinsurance business, primarily consisting of securities accounted for as available-for-sale and insurance separate account assets, which were previously included in "Financial instruments owned, at fair value" and "Securities segregated for regulatory and other purposes," respectively. See Note 12 to the consolidated financial statements for further information about assets held for sale.

Goodwill and Identifiable Intangible Assets

Goodwill. Goodwill is the cost of acquired companies in excess of the fair value of net assets, including identifiable intangible assets, at the acquisition date. Goodwill is assessed annually for impairment, or more frequently if events occur or circumstances change that indicate an impairment may exist, by first assessing qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the results of the qualitative assessment are not conclusive, a quantitative goodwill impairment test is performed by comparing the estimated fair value of each reporting unit with its estimated net book value.

Estimating the fair value of our reporting units requires management to make judgments. Critical inputs to the fair value estimates include (i) projected earnings, (ii) estimated long-term growth rates and (iii) cost of equity. The net book value of each reporting unit reflects an allocation of total shareholders' equity and represents the estimated amount of shareholders' equity required to support the activities of the reporting unit under guidelines issued by the Basel Committee on Banking Supervision (Basel Committee) in December 2010.

Our market capitalization was below book value during 2012. Accordingly, we performed a quantitative impairment test during the fourth quarter of 2012 and determined that goodwill was not impaired. The estimated fair value of our reporting units in which we hold substantially all of our goodwill significantly exceeded the estimated carrying values. We believe that it is appropriate to consider market capitalization, among other factors, as an indicator of fair value over a reasonable period of time.

If the more recent improvement in market conditions does not continue, and we return to a prolonged period of weakness in the business environment or financial markets, our goodwill could be impaired in the future. In addition, significant changes to critical inputs of the goodwill impairment test (e.g., cost of equity) could cause the estimated fair value of our reporting units to decline, which could result in an impairment of goodwill in the future.

See Note 13 to the consolidated financial statements for further information about our goodwill.

Identifiable Intangible Assets. We amortize our identifiable intangible assets (i) over their estimated lives, (ii) based on economic usage or (iii) in proportion to estimated gross profits or premium revenues. Identifiable intangible assets are tested for impairment whenever events or changes in circumstances suggest that an asset's or asset group's carrying value may not be fully recoverable.

An impairment loss, generally calculated as the difference between the estimated fair value and the carrying value of an asset or asset group, is recognized if the sum of the estimated undiscounted cash flows relating to the asset or asset group is less than the corresponding carrying value. See Note 13 to the consolidated financial statements for the carrying value and estimated remaining lives of our identifiable intangible assets by major asset class and impairments of our identifiable intangible assets.

A prolonged period of market weakness could adversely impact our businesses and impair the value of our identifiable intangible assets. In addition, certain events could indicate a potential impairment of our identifiable intangible assets, including (i) decreases in revenues from commodity-related customer contracts and relationships, (ii) decreases in cash receipts from television broadcast royalties, (iii) an adverse action or assessment by a regulator or (iv) adverse actual experience on the contracts in our variable annuity and life insurance business. Management judgment is required to evaluate whether indications of potential impairment have occurred, and to test intangibles for impairment if required.

Use of Estimates

The use of generally accepted accounting principles requires management to make certain estimates and assumptions. In addition to the estimates we make in connection with fair value measurements, and the accounting for goodwill and identifiable intangible assets, the use of estimates and assumptions is also important in determining provisions for losses that may arise from litigation, regulatory proceedings and tax audits.

We estimate and provide for potential losses that may arise out of litigation and regulatory proceedings to the extent that such losses are probable and can be reasonably estimated. In accounting for income taxes, we estimate and provide for potential liabilities that may arise out of tax audits to the extent that uncertain tax positions fail to meet the recognition standard under FASB Accounting Standards Codification 740. See Note 24 to the consolidated financial statements for further information about accounting for income taxes.

Significant judgment is required in making these estimates and our final liabilities may ultimately be materially different. Our total estimated liability in respect of litigation and regulatory proceedings is determined on a case-by-case basis and represents an estimate of probable losses after considering, among other factors, the progress of each case or proceeding, our experience and the experience of others in similar cases or proceedings, and the opinions and views of legal counsel. See Notes 18 and 27 to the consolidated financial statements for information on certain judicial, regulatory and legal proceedings.

Results of Operations

The composition of our net revenues has varied over time as financial markets and the scope of our operations have changed. The composition of net revenues can also vary over the shorter term due to fluctuations in U.S. and global economic and market conditions. See "Certain Risk Factors That May Affect Our Businesses" below and "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K for a further discussion of the impact of economic and market conditions on our results of operations.

Financial Overview

The table below presents an overview of our financial results.

	Year Ended December		
$ in millions, except per share amounts	**2012**	2011	2010
Net revenues	**$34,163**	$28,811	$39,161
Pre-tax earnings	**11,207**	6,169	12,892
Net earnings	**7,475**	4,442	8,354
Net earnings applicable to common shareholders	**7,292**	2,510	7,713
Diluted earnings per common share	**14.13**	4.51 [2]	13.18 [3]
Return on average common shareholders' equity [1]	**10.7%**	3.7% [2]	11.5% [3]

1. ROE is computed by dividing net earnings applicable to common shareholders by average monthly common shareholders' equity. The table below presents our average common shareholders' equity.

	Average for the Year Ended December		
in millions	**2012**	2011	2010
Total shareholders' equity	**$72,530**	$72,708	$74,257
Preferred stock	**(4,392)**	(3,990)	(6,957)
Common shareholders' equity	**$68,138**	$68,718	$67,300

2. Excluding the impact of the preferred dividend of $1.64 billion in the first quarter of 2011 (calculated as the difference between the carrying value and the redemption value of the preferred stock), related to the redemption of our Series G Preferred Stock, diluted earnings per common share were $7.46 and ROE was 5.9% for 2011. We believe that presenting our results for 2011 excluding this dividend is meaningful, as it increases the comparability of period-to-period results. Diluted earnings per common share and ROE excluding this dividend are non-GAAP measures and may not be comparable to similar non-GAAP measures used by other companies. The tables below present the calculation of net earnings applicable to common shareholders, diluted earnings per common share and average common shareholders' equity excluding the impact of this dividend.

in millions, except per share amount	Year Ended December 2011
Net earnings applicable to common shareholders	$ 2,510
Impact of the Series G Preferred Stock dividend	1,643
Net earnings applicable to common shareholders, excluding the impact of the Series G Preferred Stock dividend	4,153
Divided by: average diluted common shares outstanding	556.9
Diluted earnings per common share, excluding the impact of the Series G Preferred Stock dividend	$ 7.46

in millions	Average for the Year Ended December 2011
Total shareholders' equity	$72,708
Preferred stock	(3,990)
Common shareholders' equity	68,718
Impact of the Series G Preferred Stock dividend	1,264
Common shareholders' equity, excluding the impact of the Series G Preferred Stock dividend	$69,982

3. Excluding the impact of the $465 million related to the U.K. bank payroll tax, the $550 million related to the SEC settlement and the $305 million impairment of our NYSE DMM rights, diluted earnings per common share were $15.22 and ROE was 13.1% for 2010. We believe that presenting our results for 2010 excluding the impact of these items is meaningful, as it increases the comparability of period-to-period results. Diluted earnings per common share and ROE excluding these items are non-GAAP measures and may not be comparable to similar non-GAAP measures used by other companies. The tables below present the calculation of net earnings applicable to common shareholders, diluted earnings per common share and average common shareholders' equity excluding the impact of these items.

in millions, except per share amount	Year Ended December 2010
Net earnings applicable to common shareholders	$ 7,713
Impact of the U.K. bank payroll tax	465
Pre-tax impact of the SEC settlement	550
Tax impact of the SEC settlement	(6)
Pre-tax impact of the NYSE DMM rights impairment	305
Tax impact of the NYSE DMM rights impairment	(118)
Net earnings applicable to common shareholders, excluding the impact of the U.K. bank payroll tax, the SEC settlement and the NYSE DMM rights impairment	8,909
Divided by: average diluted common shares outstanding	585.3
Diluted earnings per common share, excluding the impact of the U.K. bank payroll tax, the SEC settlement and the NYSE DMM rights impairment	$ 15.22

in millions	Average for the Year Ended December 2010
Total shareholders' equity	$74,257
Preferred stock	(6,957)
Common shareholders' equity	67,300
Impact of the U.K. bank payroll tax	359
Impact of the SEC settlement	293
Impact of the NYSE DMM rights impairment	14
Common shareholders' equity, excluding the impact of the U.K. bank payroll tax, the SEC settlement and the NYSE DMM rights impairment	$67,966

Net Revenues

2012 versus 2011. Net revenues on the consolidated statements of earnings were $34.16 billion for 2012, 19% higher than 2011, reflecting significantly higher other principal transactions revenues, as well as higher market-making revenues, investment banking revenues and investment management revenues compared with 2011. These increases were partially offset by significantly lower net interest income and lower commissions and fees compared with 2011.

2011 versus 2010. Net revenues on the consolidated statements of earnings were $28.81 billion for 2011, 26% lower than 2010, reflecting significantly lower other principal transactions revenues and market-making revenues, as well as lower investment banking revenues and net interest income. These decreases were partially offset by higher commissions and fees compared with 2010. Investment management revenues were essentially unchanged compared with 2010.

Non-interest Revenues

Investment banking

During 2012, investment banking revenues reflected an operating environment generally characterized by continued concerns about the outlook for the global economy and political uncertainty. These concerns weighed on investment banking activity, as completed mergers and acquisitions activity declined compared with 2011, and equity and equity-related underwriting activity remained low, particularly in initial public offerings. However, industry-wide debt underwriting activity improved compared with 2011, as credit spreads tightened and interest rates remained low. If macroeconomic concerns continue and result in lower levels of client activity, investment banking revenues would likely be negatively impacted.

2012 versus 2011. Investment banking revenues on the consolidated statements of earnings were $4.94 billion for 2012, 13% higher than 2011, reflecting significantly higher revenues in our underwriting business, due to strong revenues in debt underwriting. Revenues in debt underwriting were significantly higher compared with 2011, primarily reflecting higher revenues from investment-grade and leveraged finance activity. Revenues in equity underwriting were lower compared with 2011, primarily reflecting a decline in industry-wide initial public offerings. Revenues in financial advisory were essentially unchanged compared with 2011.

2011 versus 2010. Investment banking revenues on the consolidated statements of earnings were $4.36 billion for 2011, 9% lower than 2010, primarily reflecting lower revenues in our underwriting business. Revenues in equity underwriting were significantly lower than 2010, principally due to a decline in industry-wide activity. Revenues in debt underwriting were essentially unchanged compared with 2010. Revenues in financial advisory decreased slightly compared with 2010.

Investment management

During 2012, investment management revenues reflected an operating environment generally characterized by improved asset prices, resulting in appreciation in the value of client assets. However, the mix of assets under supervision has shifted slightly from asset classes that typically generate higher fees to asset classes that typically generate lower fees compared with 2011. In the future, if asset prices were to decline, or investors continue to favor asset classes that typically generate lower fees or investors continue to withdraw their assets, investment management revenues would likely be negatively impacted. In addition, continued concerns about the global economic outlook could result in downward pressure on assets under supervision.

2012 versus 2011. Investment management revenues on the consolidated statements of earnings were $4.97 billion for 2012, 6% higher compared with 2011, due to significantly higher incentive fees, partially offset by slightly lower management and other fees.

2011 versus 2010. Investment management revenues on the consolidated statements of earnings were $4.69 billion for 2011, essentially unchanged compared with 2010, primarily due to higher management and other fees, reflecting favorable changes in the mix of assets under management, offset by lower incentive fees.

Commissions and fees

Although global equity prices increased during 2012, commissions and fees reflected an operating environment characterized by lower market volumes primarily due to lower volatility levels, concerns about the outlook for the global economy and continued political uncertainty. If macroeconomic concerns continue and result in lower market volumes, commissions and fees would likely continue to be negatively impacted.

2012 versus 2011. Commissions and fees on the consolidated statements of earnings were $3.16 billion for 2012, 16% lower than 2011, reflecting lower market volumes.

2011 versus 2010. Commissions and fees on the consolidated statements of earnings were $3.77 billion for 2011, 6% higher than 2010, primarily reflecting higher market volumes, particularly during the third quarter of 2011.

Market making

During 2012, market-making revenues reflected an operating environment generally characterized by continued broad market concerns and uncertainties, although positive developments helped to improve market conditions. These developments included certain central bank actions to ease monetary policy and address funding risks for European financial institutions. In addition, the U.S. economy posted stable to improving economic data, including favorable developments in unemployment and housing. These improvements resulted in tighter credit spreads, higher global equity prices and lower levels of volatility. However, concerns about the outlook for the global economy and continued political uncertainty, particularly the political debate in the United States surrounding the fiscal cliff, generally resulted in client risk aversion and lower activity levels. Also, uncertainty over financial regulatory reform persisted. If these concerns and uncertainties continue over the long term, market-making revenues would likely be negatively impacted.

2012 versus 2011. Market-making revenues on the consolidated statements of earnings were $11.35 billion for 2012, 22% higher than 2011, primarily reflecting significantly higher revenues in mortgages and higher revenues in interest rate products, credit products and equity cash products, partially offset by significantly lower revenues in commodities. In addition, market-making revenues included significantly higher revenues in securities services compared with 2011, reflecting a gain of approximately $500 million on the sale of our hedge fund administration business.

2011 versus 2010. Market-making revenues on the consolidated statements of earnings were $9.29 billion for 2011, 32% lower than 2010. Although activity levels during 2011 were generally consistent with 2010 levels, and results were solid during the first quarter of 2011, the environment during the remainder of 2011 was characterized by broad market concerns and uncertainty, resulting in volatile markets and significantly wider credit spreads, which contributed to difficult market-making conditions and led to reductions in risk by us and our clients. As a result of these conditions, revenues across most of our major market-making activities were lower during 2011 compared with 2010.

Other principal transactions

During 2012, other principal transactions revenues reflected an operating environment characterized by tighter credit spreads and an increase in global equity prices. However, concerns about the outlook for the global economy and uncertainty over financial regulatory reform persisted. If equity markets decline or credit spreads widen, other principal transactions revenues would likely be negatively impacted.

2012 versus 2011. Other principal transactions revenues on the consolidated statements of earnings were $5.87 billion and $1.51 billion for 2012 and 2011, respectively. Results for 2012 included a gain from our investment in the ordinary shares of ICBC, net gains from other investments in equities, primarily in private equities, net gains from debt securities and loans, and revenues related to our consolidated investment entities.

2011 versus 2010. Other principal transactions revenues on the consolidated statements of earnings were $1.51 billion and $6.93 billion for 2011 and 2010, respectively. Results for 2011 included a loss from our investment in the ordinary shares of ICBC and net gains from other investments in equities, primarily in private equities, partially offset by losses from public equities. In addition, revenues in other principal transactions included net losses from debt securities and loans, primarily reflecting approximately $1 billion of unrealized losses related to relationship lending activities, including the effect of hedges, partially offset by net gains from other debt securities and loans. Results for 2011 also included revenues related to our consolidated investment entities. Results for 2010 included a gain from our investment in the ordinary shares of ICBC, net gains from other investments in equities, net gains from debt securities and loans, and revenues related to consolidated investment entities.

Net Interest Income

2012 versus 2011. Net interest income on the consolidated statements of earnings was $3.88 billion for 2012, 25% lower than 2011. The decrease compared with 2011 was primarily due to lower average yields on financial instruments owned, at fair value, and collateralized agreements.

2011 versus 2010. Net interest income on the consolidated statements of earnings was $5.19 billion for 2011, 6% lower than 2010. The decrease compared with 2010 was primarily due to higher interest expense related to our long-term borrowings and higher dividend expense related to financial instruments sold, but not yet purchased, partially offset by an increase in interest income from higher yielding collateralized agreements.

Operating Expenses

Our operating expenses are primarily influenced by compensation, headcount and levels of business activity. Compensation and benefits includes salaries, discretionary compensation, amortization of equity awards and other items such as benefits. Discretionary compensation is significantly impacted by, among other factors, the level of net revenues, overall financial performance, prevailing labor markets, business mix, the structure of our share-based compensation programs and the external environment.

In the context of more difficult economic and financial conditions, the firm launched an initiative during the second quarter of 2011 to identify areas where we can operate more efficiently and reduce our operating expenses. During 2012 and 2011, we announced targeted annual run rate compensation and non-compensation reductions of approximately $1.9 billion in aggregate.

The table below presents our operating expenses and total staff.

	Year Ended December		
$ in millions	**2012**	2011	2010
Compensation and benefits	**$12,944**	$12,223	$15,376
U.K. bank payroll tax	**—**	—	465
Brokerage, clearing, exchange and distribution fees	**2,208**	2,463	2,281
Market development	**509**	640	530
Communications and technology	**782**	828	758
Depreciation and amortization	**1,738**	1,865	1,889
Occupancy	**875**	1,030	1,086
Professional fees	**867**	992	927
Insurance reserves [1]	**598**	529	398
Other expenses	**2,435**	2,072	2,559
Total non-compensation expenses	**10,012**	10,419	10,428
Total operating expenses	**$22,956**	$22,642	$26,269
Total staff at period-end [2]	**32,400**	33,300	35,700

1. Related revenues are included in "Market making" on the consolidated statements of earnings.

2. Includes employees, consultants and temporary staff.

2012 versus 2011. Operating expenses on the consolidated statements of earnings were $22.96 billion for 2012, essentially unchanged compared with 2011. Compensation and benefits expenses on the consolidated statements of earnings were $12.94 billion for 2012, 6% higher compared with $12.22 billion for 2011. The ratio of compensation and benefits to net revenues for 2012 was 37.9%, compared with 42.4% for 2011. Total staff decreased 3% during 2012.

Non-compensation expenses on the consolidated statements of earnings were $10.01 billion for 2012, 4% lower compared with 2011. The decrease compared with 2011 primarily reflected the impact of expense reduction initiatives, lower brokerage, clearing, exchange and distribution fees, lower occupancy expenses and lower impairment charges. These decreases were partially offset by higher other expenses and increased reserves related to our reinsurance business. The increase in other expenses compared with 2011 primarily reflected higher net provisions for litigation and regulatory proceedings and higher charitable contributions. Net provisions for litigation and regulatory proceedings were $448 million during 2012 (including a settlement with the Board of Governors of the Federal Reserve System (Federal Reserve Board) regarding the independent foreclosure review). Charitable contributions were $225 million during 2012, including $159 million to Goldman Sachs Gives, our donor-advised fund, and $10 million to The Goldman Sachs Foundation. Compensation was reduced to fund the charitable contribution to Goldman Sachs Gives. The firm asks its participating managing directors to make recommendations regarding potential charitable recipients for this contribution.

2011 versus 2010. Operating expenses on the consolidated statements of earnings were $22.64 billion for 2011, 14% lower than 2010. Compensation and benefits expenses on the consolidated statements of earnings were $12.22 billion for 2011, a 21% decline compared with $15.38 billion for 2010. The ratio of compensation and benefits to net revenues for 2011 was 42.4%, compared with 39.3% [1] (which excludes the impact of the U.K. bank payroll tax) for 2010. Operating expenses for 2010 included $465 million related to the U.K. bank payroll tax. Total staff decreased 7% during 2011.

Non-compensation expenses on the consolidated statements of earnings were $10.42 billion for 2011, essentially unchanged compared with 2010. Non-compensation expenses for 2011 included higher brokerage, clearing, exchange and distribution fees, increased reserves related to our reinsurance business and higher market development expenses compared with 2010. These increases were offset by lower other expenses during 2011. The decrease in other expenses primarily reflected lower net provisions for litigation and regulatory proceedings (2010 included $550 million related to a settlement with the SEC). In addition, non-compensation expenses during 2011 included impairment charges of approximately $440 million, primarily related to consolidated investments and Litton Loan Servicing LP. Charitable contributions were $163 million during 2011, including $78 million to Goldman Sachs Gives and $25 million to The Goldman Sachs Foundation. Compensation was reduced to fund the charitable contribution to Goldman Sachs Gives. The firm asks its participating managing directors to make recommendations regarding potential charitable recipients for this contribution.

1. We believe that presenting our ratio of compensation and benefits to net revenues excluding the impact of the $465 million U.K. bank payroll tax is meaningful, as excluding it increases the comparability of period-to-period results. The ratio of compensation and benefits to net revenues excluding the impact of this item is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies. The table below presents the calculation of the ratio of compensation and benefits to net revenues including and excluding the impact of this item.

$ in millions	Year Ended December 2010
Compensation and benefits (which excludes the impact of the $465 million U.K. bank payroll tax)	$15,376
Ratio of compensation and benefits to net revenues	39.3%
Compensation and benefits, including the impact of the $465 million U.K. bank payroll tax	$15,841
Ratio of compensation and benefits to net revenues, including the impact of the $465 million U.K. bank payroll tax	40.5%

Provision for Taxes

The effective income tax rate for 2012 was 33.3%, up from 28.0% for 2011. The increase from 28.0% to 33.3% was primarily due to the earnings mix and a decrease in the impact of permanent benefits.

The effective income tax rate for 2011 was 28.0%, down from 35.2% for 2010. Excluding the impact of the $465 million U.K. bank payroll tax and the $550 million SEC settlement, substantially all of which was non-deductible, the effective income tax rate for 2010 was 32.7% [1]. The decrease from 32.7% to 28.0% was primarily due to an increase in permanent benefits as a percentage of earnings and the earnings mix.

1. We believe that presenting our effective income tax rate for 2010 excluding the impact of the U.K. bank payroll tax and the SEC settlement, substantially all of which was non-deductible, is meaningful as excluding these items increases the comparability of period-to-period results. The effective income tax rate excluding the impact of these items is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies. The table below presents the calculation of the effective income tax rate excluding the impact of these amounts.

	Year Ended December 2010		
$ in millions	Pre-tax earnings	Provision for taxes	Effective income tax rate
As reported	$12,892	$4,538	35.2%
Add back:			
Impact of the U.K. bank payroll tax	465	—	
Impact of the SEC settlement	550	6	
As adjusted	$13,907	$4,544	32.7%

Segment Operating Results

The table below presents the net revenues, operating expenses and pre-tax earnings of our segments.

in millions		Year Ended December 2012	2011	2010
Investment Banking	Net revenues	**$ 4,926**	$ 4,355	$ 4,810
	Operating expenses	**3,330**	2,995	3,459
	Pre-tax earnings	**$ 1,596**	$ 1,360	$ 1,351
Institutional Client Services	Net revenues	**$18,124**	$17,280	$21,796
	Operating expenses	**12,480**	12,837	14,994
	Pre-tax earnings	**$ 5,644**	$ 4,443	$ 6,802
Investing & Lending	Net revenues	**$ 5,891**	$ 2,142	$ 7,541
	Operating expenses	**2,666**	2,673	3,361
	Pre-tax earnings/(loss)	**$ 3,225**	$ (531)	$ 4,180
Investment Management	Net revenues	**$ 5,222**	$ 5,034	$ 5,014
	Operating expenses	**4,294**	4,020	4,082
	Pre-tax earnings	**$ 928**	$ 1,014	$ 932
Total	**Net revenues**	**$34,163**	$28,811	$39,161
	Operating expenses	**22,956**	22,642	26,269
	Pre-tax earnings	**$11,207**	$ 6,169	$12,892

Total operating expenses in the table above include the following expenses that have not been allocated to our segments:

- charitable contributions of $169 million, $103 million and $345 million for the years ended December 2012, December 2011 and December 2010, respectively; and
- real estate-related exit costs of $17 million, $14 million and $28 million for the years ended December 2012, December 2011 and December 2010, respectively. Real estate-related exit costs are included in "Depreciation and amortization" and "Occupancy" in the consolidated statements of earnings.

Operating expenses related to net provisions for litigation and regulatory proceedings, previously not allocated to our segments, have now been allocated. This allocation is consistent with the manner in which management currently views the performance of our segments. Reclassifications have been made to previously reported segment amounts to conform to the current presentation.

Net revenues in our segments include allocations of interest income and interest expense to specific securities, commodities and other positions in relation to the cash generated by, or funding requirements of, such underlying positions. See Note 25 to the consolidated financial statements for further information about our business segments.

The cost drivers of Goldman Sachs taken as a whole — compensation, headcount and levels of business activity — are broadly similar in each of our business segments. Compensation and benefits expenses within our segments reflect, among other factors, the overall performance of Goldman Sachs as well as the performance of individual businesses. Consequently, pre-tax margins in one segment of our business may be significantly affected by the performance of our other business segments. A discussion of segment operating results follows.

Investment Banking

Our Investment Banking segment is comprised of:

Financial Advisory. Includes strategic advisory assignments with respect to mergers and acquisitions, divestitures, corporate defense activities, risk management, restructurings and spin-offs, and derivative transactions directly related to these client advisory assignments.

Underwriting. Includes public offerings and private placements, including domestic and cross-border transactions, of a wide range of securities, loans and other financial instruments, and derivative transactions directly related to these client underwriting activities.

The table below presents the operating results of our Investment Banking segment.

	Year Ended December		
in millions	**2012**	2011	2010
Financial Advisory	**$1,975**	$1,987	$2,062
Equity underwriting	**987**	1,085	1,462
Debt underwriting	**1,964**	1,283	1,286
Total Underwriting	**2,951**	2,368	2,748
Total net revenues	**4,926**	4,355	4,810
Operating expenses	**3,330**	2,995	3,459
Pre-tax earnings	**$1,596**	$1,360	$1,351

The table below presents our financial advisory and underwriting transaction volumes. [1]

	Year Ended December		
in billions	**2012**	2011	2010
Announced mergers and acquisitions	**$707**	$634	$500
Completed mergers and acquisitions	**574**	652	441
Equity and equity-related offerings [2]	**57**	55	67
Debt offerings [3]	**236**	206	234

1. Source: Thomson Reuters. Announced and completed mergers and acquisitions volumes are based on full credit to each of the advisors in a transaction. Equity and equity-related offerings and debt offerings are based on full credit for single book managers and equal credit for joint book managers. Transaction volumes may not be indicative of net revenues in a given period. In addition, transaction volumes for prior periods may vary from amounts previously reported due to the subsequent withdrawal or a change in the value of a transaction.
2. Includes Rule 144A and public common stock offerings, convertible offerings and rights offerings.
3. Includes non-convertible preferred stock, mortgage-backed securities, asset-backed securities and taxable municipal debt. Includes publicly registered and Rule 144A issues. Excludes leveraged loans.

2012 versus 2011. Net revenues in Investment Banking were $4.93 billion for 2012, 13% higher than 2011.

Net revenues in Financial Advisory were $1.98 billion, essentially unchanged compared with 2011. Net revenues in our Underwriting business were $2.95 billion, 25% higher than 2011, due to strong net revenues in debt underwriting. Net revenues in debt underwriting were significantly higher compared with 2011, primarily reflecting higher net revenues from investment-grade and leveraged finance activity. Net revenues in equity underwriting were lower compared with 2011, primarily reflecting a decline in industry-wide initial public offerings.

During 2012, Investment Banking operated in an environment generally characterized by continued concerns about the outlook for the global economy and political uncertainty. These concerns weighed on investment banking activity, as completed mergers and acquisitions activity declined compared with 2011, and equity and equity-related underwriting activity remained low, particularly in initial public offerings. However, industry-wide debt underwriting activity improved compared with 2011, as credit spreads tightened and interest rates remained low. If macroeconomic concerns continue and result in lower levels of client activity, net revenues in Investment Banking would likely be negatively impacted.

Our investment banking transaction backlog increased compared with the end of 2011. The increase compared with the end of 2011 was due to an increase in potential debt underwriting transactions, primarily reflecting an increase in leveraged finance transactions, and an increase in potential advisory transactions. These increases were partially offset by a decrease in potential equity underwriting transactions compared with the end of 2011, reflecting uncertainty in market conditions.

Our investment banking transaction backlog represents an estimate of our future net revenues from investment banking transactions where we believe that future revenue realization is more likely than not. We believe changes in our investment banking transaction backlog may be a useful indicator of client activity levels which, over the long term, impact our net revenues. However, the time frame for completion and corresponding revenue recognition of transactions in our backlog varies based on the nature of the assignment, as certain transactions may remain in our backlog for longer periods of time and others may enter and leave within the same reporting period. In addition, our transaction backlog is subject to certain limitations, such as assumptions about the likelihood that individual client transactions will occur in the future. Transactions may be cancelled or modified, and transactions not included in the estimate may also occur.

Operating expenses were $3.33 billion for 2012, 11% higher than 2011, due to increased compensation and benefits expenses, primarily resulting from higher net revenues. Pre-tax earnings were $1.60 billion in 2012, 17% higher than 2011.

2011 versus 2010. Net revenues in Investment Banking were $4.36 billion for 2011, 9% lower than 2010.

Net revenues in Financial Advisory were $1.99 billion, 4% lower than 2010. Net revenues in our Underwriting business were $2.37 billion, 14% lower than 2010, reflecting significantly lower net revenues in equity underwriting, principally due to a decline in industry-wide activity. Net revenues in debt underwriting were essentially unchanged compared with 2010.

Investment Banking operated in an environment generally characterized by significant declines in industry-wide underwriting and mergers and acquisitions activity levels during the second half of 2011. These declines reflected increased concerns regarding the weakened state of global economies, including heightened European sovereign debt risk, which contributed to a significant widening in credit spreads, a sharp increase in volatility levels and a significant decline in global equity markets during the second half of 2011.

Our investment banking transaction backlog increased compared with the end of 2010. The increase compared with the end of 2010 was due to an increase in potential equity underwriting transactions, primarily reflecting an increase in client mandates to underwrite initial public offerings. Estimated net revenues from potential debt underwriting transactions decreased slightly compared with the end of 2010. Estimated net revenues from potential advisory transactions were essentially unchanged compared with the end of 2010.

Operating expenses were $3.00 billion for 2011, 13% lower than 2010, due to decreased compensation and benefits expenses, primarily resulting from lower net revenues. Pre-tax earnings were $1.36 billion in 2011, essentially unchanged compared with 2010.

Institutional Client Services

Our Institutional Client Services segment is comprised of:

Fixed Income, Currency and Commodities Client Execution. Includes client execution activities related to making markets in interest rate products, credit products, mortgages, currencies and commodities.

We generate market-making revenues in these activities, in three ways:

- In large, highly liquid markets (such as markets for U.S. Treasury bills or certain mortgage pass-through certificates), we execute a high volume of transactions for our clients for modest spreads and fees.
- In less liquid markets (such as mid-cap corporate bonds, growth market currencies or certain non-agency mortgage-backed securities), we execute transactions for our clients for spreads and fees that are generally somewhat larger.
- We also structure and execute transactions involving customized or tailor-made products that address our clients' risk exposures, investment objectives or other complex needs (such as a jet fuel hedge for an airline).

Given the focus on the mortgage market, our mortgage activities are further described below.

Our activities in mortgages include commercial mortgage-related securities, loans and derivatives, residential mortgage-related securities, loans and derivatives (including U.S. government agency-issued collateralized mortgage obligations, other prime, subprime and Alt-A securities and loans), and other asset-backed securities, loans and derivatives.

We buy, hold and sell long and short mortgage positions, primarily for market making for our clients. Our inventory therefore changes based on client demands and is generally held for short-term periods.

See Notes 18 and 27 to the consolidated financial statements for information about exposure to mortgage repurchase requests, mortgage rescissions and mortgage-related litigation.

Equities. Includes client execution activities related to making markets in equity products, as well as commissions and fees from executing and clearing institutional client transactions on major stock, options and futures exchanges worldwide. Equities also includes our securities services business, which provides financing, securities lending and other prime brokerage services to institutional clients, including hedge funds, mutual funds, pension funds and foundations, and generates revenues primarily in the form of interest rate spreads or fees, and revenues related to our reinsurance activities.

The table below presents the operating results of our Institutional Client Services segment.

in millions	Year Ended December 2012	2011	2010
Fixed Income, Currency and Commodities Client Execution	$ 9,914	$ 9,018	$13,707
Equities client execution [1]	3,171	3,031	3,231
Commissions and fees	3,053	3,633	3,426
Securities services	1,986	1,598	1,432
Total Equities	8,210	8,262	8,089
Total net revenues	18,124	17,280	21,796
Operating expenses	12,480	12,837	14,994
Pre-tax earnings	$ 5,644	$ 4,443	$ 6,802

1. Includes net revenues related to reinsurance of $1.08 billion, $880 million and $827 million for the years ended December 2012, December 2011 and December 2010, respectively.

2012 versus 2011. Net revenues in Institutional Client Services were $18.12 billion for 2012, 5% higher than 2011.

Net revenues in Fixed Income, Currency and Commodities Client Execution were $9.91 billion for 2012, 10% higher than 2011. These results reflected strong net revenues in mortgages, which were significantly higher compared with 2011. In addition, net revenues in credit products and interest rate products were solid and higher compared with 2011. These increases were partially offset by significantly lower net revenues in commodities and slightly lower net revenues in currencies. Although broad market concerns persisted during 2012, Fixed Income, Currency and Commodities Client Execution operated in a generally improved environment characterized by tighter credit spreads and less challenging market-making conditions compared with 2011.

Net revenues in Equities were $8.21 billion for 2012, essentially unchanged compared with 2011. Net revenues in securities services were significantly higher compared with 2011, reflecting a gain of approximately $500 million on the sale of our hedge fund administration business. In addition, equities client execution net revenues were higher than 2011, primarily reflecting significantly higher results in cash products, principally due to increased levels of client activity. These increases were offset by lower commissions and fees, reflecting lower market volumes. During 2012, Equities operated in an environment generally characterized by an increase in global equity prices and lower volatility levels.

The net loss attributable to the impact of changes in our own credit spreads on borrowings for which the fair value option was elected was $714 million ($433 million and $281 million related to Fixed Income, Currency and Commodities Client Execution and equities client execution, respectively) for 2012, compared with a net gain of $596 million ($399 million and $197 million related to Fixed Income, Currency and Commodities Client Execution and equities client execution, respectively) for 2011.

During 2012, Institutional Client Services operated in an environment generally characterized by continued broad market concerns and uncertainties, although positive developments helped to improve market conditions. These developments included certain central bank actions to ease monetary policy and address funding risks for European financial institutions. In addition, the U.S. economy posted stable to improving economic data, including favorable developments in unemployment and housing. These improvements resulted in tighter credit spreads, higher global equity prices and lower levels of volatility. However, concerns about the outlook for the global economy and continued political uncertainty, particularly the political debate in the United States surrounding the fiscal cliff, generally resulted in client risk aversion and lower activity levels. Also, uncertainty over financial regulatory reform persisted. If these concerns and uncertainties continue over the long term, net revenues in Fixed Income, Currency and Commodities Client Execution and Equities would likely be negatively impacted.

Operating expenses were $12.48 billion for 2012, 3% lower than 2011, primarily due to lower brokerage, clearing, exchange and distribution fees, and lower impairment charges, partially offset by higher net provisions for litigation and regulatory proceedings. Pre-tax earnings were $5.64 billion in 2012, 27% higher than 2011.

2011 versus 2010. Net revenues in Institutional Client Services were $17.28 billion for 2011, 21% lower than 2010.

Net revenues in Fixed Income, Currency and Commodities Client Execution were $9.02 billion for 2011, 34% lower than 2010. Although activity levels during 2011 were generally consistent with 2010 levels, and results were solid during the first quarter of 2011, the environment during the remainder of 2011 was characterized by broad market concerns and uncertainty, resulting in volatile markets and significantly wider credit spreads, which contributed to difficult market-making conditions and led to reductions in risk by us and our clients. As a result of these conditions, net revenues across the franchise were lower, including significant declines in mortgages and credit products, compared with 2010.

Net revenues in Equities were $8.26 billion for 2011, 2% higher than 2010. During 2011, average volatility levels increased and equity prices in Europe and Asia declined significantly, particularly during the third quarter. The increase in net revenues reflected higher commissions and fees, primarily due to higher market volumes, particularly during the third quarter of 2011. In addition, net revenues in securities services increased compared with 2010, reflecting the impact of higher average customer balances. Equities client execution net revenues were lower than 2010, primarily reflecting significantly lower net revenues in shares.

The net gain attributable to the impact of changes in our own credit spreads on borrowings for which the fair value option was elected was $596 million ($399 million and $197 million related to Fixed Income, Currency and Commodities Client Execution and equities client execution, respectively) for 2011, compared with a net gain of $198 million ($188 million and $10 million related to Fixed Income, Currency and Commodities Client Execution and equities client execution, respectively) for 2010.

Institutional Client Services operated in an environment generally characterized by increased concerns regarding the weakened state of global economies, including heightened European sovereign debt risk, and its impact on the European banking system and global financial institutions. These conditions also impacted expectations for economic prospects in the United States and were reflected in equity and debt markets more broadly. In addition, the downgrade in credit ratings of the U.S. government and federal agencies and many financial institutions during the second half of 2011 contributed to further uncertainty in the markets. These concerns, as well as other broad market concerns, such as uncertainty over financial regulatory reform, continued to have a negative impact on our net revenues during 2011.

Operating expenses were $12.84 billion for 2011, 14% lower than 2010, due to decreased compensation and benefits expenses, primarily resulting from lower net revenues, lower net provisions for litigation and regulatory proceedings (2010 included $550 million related to a settlement with the SEC), the impact of the U.K. bank payroll tax during 2010, as well as an impairment of our NYSE DMM rights of $305 million during 2010. These decreases were partially offset by higher brokerage, clearing, exchange and distribution fees, principally reflecting higher transaction volumes in Equities. Pre-tax earnings were $4.44 billion in 2011, 35% lower than 2010.

Investing & Lending

Investing & Lending includes our investing activities and the origination of loans to provide financing to clients. These investments and loans are typically longer-term in nature. We make investments, directly and indirectly through funds that we manage, in debt securities and loans, public and private equity securities, real estate, consolidated investment entities and power generation facilities.

The table below presents the operating results of our Investing & Lending segment.

	Year Ended December		
in millions	**2012**	2011	2010
ICBC	**$ 408**	$ (517)	$ 747
Equity securities (excluding ICBC)	**2,392**	1,120	2,692
Debt securities and loans	**1,850**	96	2,597
Other	**1,241**	1,443	1,505
Total net revenues	**5,891**	2,142	7,541
Operating expenses	**2,666**	2,673	3,361
Pre-tax earnings/(loss)	**$3,225**	$ (531)	$4,180

2012 versus 2011. Net revenues in Investing & Lending were $5.89 billion and $2.14 billion for 2012 and 2011, respectively. During 2012, Investing & Lending net revenues were positively impacted by tighter credit spreads and an increase in global equity prices. Results for 2012 included a gain of $408 million from our investment in the ordinary shares of ICBC, net gains of $2.39 billion from other investments in equities, primarily in private equities, net gains and net interest income of $1.85 billion from debt securities and loans, and other net revenues of $1.24 billion, principally related to our consolidated investment entities. If equity markets decline or credit spreads widen, net revenues in Investing & Lending would likely be negatively impacted.

Operating expenses were $2.67 billion for 2012, essentially unchanged compared with 2011. Pre-tax earnings were $3.23 billion in 2012, compared with a pre-tax loss of $531 million in 2011.

2011 versus 2010. Net revenues in Investing & Lending were $2.14 billion and $7.54 billion for 2011 and 2010, respectively. During 2011, Investing & Lending results reflected an operating environment characterized by a significant decline in equity markets in Europe and Asia, and unfavorable credit markets that were negatively impacted by increased concerns regarding the weakened state of global economies, including heightened European sovereign debt risk. Results for 2011 included a loss of $517 million from our investment in the ordinary shares of ICBC and net gains of $1.12 billion from other investments in equities, primarily in private equities, partially offset by losses from public equities. In addition, Investing & Lending included net revenues of $96 million from debt securities and loans. This amount includes approximately $1 billion of unrealized losses related to relationship lending activities, including the effect of hedges, offset by net interest income and net gains from other debt securities and loans. Results for 2011 also included other net revenues of $1.44 billion, principally related to our consolidated investment entities.

Results for 2010 included a gain of $747 million from our investment in the ordinary shares of ICBC, a net gain of $2.69 billion from other investments in equities, a net gain of $2.60 billion from debt securities and loans and other net revenues of $1.51 billion, principally related to our consolidated investment entities. The net gain from other investments in equities was primarily driven by an increase in global equity markets, which resulted in appreciation of both our public and private equity positions and provided favorable conditions for initial public offerings. The net gains and net interest from debt securities and loans primarily reflected the impact of tighter credit spreads and favorable credit markets during the year, which provided favorable conditions for borrowers to refinance.

Operating expenses were $2.67 billion for 2011, 20% lower than 2010, due to decreased compensation and benefits expenses, primarily resulting from lower net revenues. This decrease was partially offset by the impact of impairment charges related to consolidated investments during 2011. Pre-tax loss was $531 million in 2011, compared with pre-tax earnings of $4.18 billion in 2010.

Investment Management

Investment Management provides investment management services and offers investment products (primarily through separately managed accounts and commingled vehicles, such as mutual funds and private investment funds) across all major asset classes to a diverse set of institutional and individual clients. Investment Management also offers wealth advisory services, including portfolio management and financial counseling, and brokerage and other transaction services to high-net-worth individuals and families.

Assets under supervision include assets under management and other client assets. Assets under management include client assets where we earn a fee for managing assets on a discretionary basis. This includes net assets in our mutual funds, hedge funds, credit funds and private equity funds (including real estate funds), and separately managed accounts for institutional and individual investors. Other client assets include client assets invested with third-party managers, private bank deposits and assets related to advisory relationships where we earn a fee for advisory and other services, but do not have discretion over the assets. Assets under supervision do not include the self-directed brokerage accounts of our clients.

Assets under management and other client assets typically generate fees as a percentage of net asset value, which vary by asset class and are affected by investment performance as well as asset inflows and redemptions.

In certain circumstances, we are also entitled to receive incentive fees based on a percentage of a fund's return or when the return exceeds a specified benchmark or other performance targets. Incentive fees are recognized only when all material contingencies are resolved.

The table below presents the operating results of our Investment Management segment.

	Year Ended December		
in millions	**2012**	2011	2010
Management and other fees	**$4,105**	$4,188	$3,956
Incentive fees	**701**	323	527
Transaction revenues	**416**	523	531
Total net revenues	**5,222**	5,034	5,014
Operating expenses	**4,294**	4,020	4,082
Pre-tax earnings	**$ 928**	$1,014	$ 932

The tables below present our assets under supervision, including assets under management by asset class and other client assets, as well as a summary of the changes in our assets under supervision.

in billions	As of December 31, 2012	2011	2010
Alternative investments [1]	**$133**	$142	$148
Equity	**133**	126	144
Fixed income	**370**	340	340
Total non-money market assets	**636**	608	632
Money markets	**218**	220	208
Total assets under management (AUM)	**854**	828	840
Other client assets	**111**	67	77
Total assets under supervision (AUS)	**$965**	$895	$917

1. Primarily includes hedge funds, credit funds, private equity, real estate, currencies, commodities and asset allocation strategies.

in billions	Year Ended December 31, 2012	2011	2010
Balance, beginning of year	**$895**	$917	$955
Net inflows/(outflows)			
Alternative investments	**(11)**	(5)	(1)
Equity	**(13)**	(9)	(21)
Fixed income	**8**	(15)	7
Total non-money market net inflows/(outflows)	**(16)**	(29)	(15)
Money markets	**(2)**	12	(56)
Total AUM net inflows/(outflows)	**(18)**	(17) [2]	(71)
Other client assets net inflows/(outflows)	**39**	(10)	(7)
Total AUS net inflows/(outflows)	**21** [1]	(27)	(78)
Net market appreciation/(depreciation)			
AUM	**44**	5	40
Other client assets	**5**	—	—
Total AUS net market appreciation/(depreciation)	**49**	5	40
Balance, end of year	**$965**	$895	$917

1. Includes $34 billion of fixed income asset inflows in connection with our acquisition of Dwight Asset Management, including $17 billion in assets under management and $17 billion in other client assets, and $5 billion of fixed income and equity asset outflows in connection with our liquidation of Goldman Sachs Asset Management Korea, all related to assets under management.

2. Includes $6 billion of asset inflows across all asset classes in connection with our acquisitions of Goldman Sachs Australia Pty Ltd and Benchmark Asset Management Company Private Limited.

2012 versus 2011. Net revenues in Investment Management were $5.22 billion for 2012, 4% higher than 2011, due to significantly higher incentive fees, partially offset by lower transaction revenues and slightly lower management and other fees. During the year, assets under supervision increased $70 billion to $965 billion. Assets under management increased $26 billion to $854 billion, reflecting net market appreciation of $44 billion, primarily in fixed income and equity assets, partially offset by net outflows of $18 billion. Net outflows in assets under management included outflows in equity, alternative investment and money market assets, partially offset by inflows in fixed income assets. Other client assets increased $44 billion to $111 billion, primarily due to net inflows, principally in client assets invested with third-party managers and assets related to advisory relationships.

During 2012, Investment Management operated in an environment generally characterized by improved asset prices, resulting in appreciation in the value of client assets. However, the mix of assets under supervision has shifted slightly from asset classes that typically generate higher fees to asset classes that typically generate lower fees compared with 2011. In the future, if asset prices were to decline, or investors continue to favor asset classes that typically generate lower fees or investors continue to withdraw their assets, net revenues in Investment Management would likely be negatively impacted. In addition, continued concerns about the global economic outlook could result in downward pressure on assets under supervision.

Operating expenses were $4.29 billion for 2012, 7% higher than 2011, due to increased compensation and benefits expenses. Pre-tax earnings were $928 million in 2012, 8% lower than 2011.

2011 versus 2010. Net revenues in Investment Management were $5.03 billion for 2011, essentially unchanged compared with 2010, primarily due to higher management and other fees, reflecting favorable changes in the mix of assets under management, offset by lower incentive fees. During 2011, assets under supervision decreased $22 billion to $895 billion. Assets under management decreased $12 billion to $828 billion, reflecting net outflows of $17 billion, partially offset by net market appreciation of $5 billion. Net outflows in assets under management primarily reflected outflows in fixed income and equity assets, partially offset by inflows in money market assets. Other client assets decreased $10 billion to $67 billion, primarily due to net outflows, principally in client assets invested with third-party managers in money market funds.

During the first half of 2011, Investment Management operated in an environment generally characterized by improved asset prices and a shift in investor assets away from money markets in favor of asset classes with potentially higher risk and returns. However, during the second half of 2011, asset prices declined, particularly in equities, in part driven by increased uncertainty regarding the global economic outlook. Declining asset prices and economic uncertainty contributed to investors shifting assets away from asset classes with potentially higher risk and returns to asset classes with lower risk and returns.

Operating expenses were $4.02 billion for 2011, 2% lower than 2010. Pre-tax earnings were $1.01 billion in 2011, 9% higher than 2010.

Geographic Data

See Note 25 to the consolidated financial statements for a summary of our total net revenues, pre-tax earnings and net earnings by geographic region.

Regulatory Developments

The U.S. Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), enacted in July 2010, significantly altered the financial regulatory regime within which we operate. The implications of the Dodd-Frank Act for our businesses will depend to a large extent on the rules that will be adopted by the Federal Reserve Board, the Federal Deposit Insurance Corporation (FDIC), the SEC, the U.S. Commodity Futures Trading Commission (CFTC) and other agencies to implement the legislation, as well as the development of market practices and structures under the regime established by the legislation and the implementing rules. Other reforms have been adopted or are being considered by other regulators and policy makers worldwide and these reforms may affect our businesses. We expect that the principal areas of impact from regulatory reform for us will be:

- the Dodd-Frank prohibition on "proprietary trading" and the limitation on the sponsorship of, and investment in, hedge funds and private equity funds by banking entities, including bank holding companies, referred to as the "Volcker Rule";
- increased regulation of and restrictions on over-the-counter (OTC) derivatives markets and transactions; and
- increased regulatory capital requirements.

In October 2011, the proposed rules to implement the Volcker Rule were issued and included an extensive request for comments on the proposal. The proposed rules are highly complex, and many aspects of the Volcker Rule remain unclear. The full impact of the rule on us will depend upon the detailed scope of the prohibitions, permitted activities, exceptions and exclusions, and will not be known with certainty until the rules are finalized and market practices and structures develop under the final rules. Currently, companies are expected to be required to be in compliance by July 2014 (subject to possible extensions).

While many aspects of the Volcker Rule remain unclear, we evaluated the prohibition on "proprietary trading" and determined that businesses that engage in "bright line" proprietary trading are most likely to be prohibited. In 2011 and 2010, we liquidated substantially all of our Principal Strategies and Global Macro Proprietary trading positions.

In addition, we have evaluated the limitations on sponsorship of, and investments in, hedge funds and private equity funds. The firm earns management fees and incentive fees for investment management services from hedge funds and private equity funds, which are included in our Investment Management segment. The firm also makes investments in funds, and the gains and losses from these investments are included in our Investing & Lending segment; these gains and losses will be impacted by the Volcker Rule. The Volcker Rule limitation on investments in hedge funds and private equity funds requires the firm to reduce its investment in each hedge fund and private equity fund to 3% or less of the fund's net asset value, and to reduce the firm's aggregate investment in all such funds to 3% or less of the firm's Tier 1 capital. The firm's aggregate net revenues from its investments in hedge funds and private equity funds were not material to the firm's aggregate total net revenues over the period from 1999 through 2012. We continue to manage our existing private equity funds, taking into account the transition periods under the Volcker Rule. With respect to our hedge funds, we currently plan to comply with the Volcker Rule by redeeming certain of our interests in the funds. Since March 2012, we have been redeeming up to approximately 10% of certain hedge funds' total redeemable units per quarter, and expect to continue to do so through June 2014. We redeemed approximately $1.06 billion of these interests in hedge funds during the year ended December 2012. In addition, we have limited the firm's initial investment to 3% for certain new investments in hedge funds and private equity funds.

As required by the Dodd-Frank Act, the Federal Reserve Board and FDIC have jointly issued a rule requiring each bank holding company with over $50 billion in assets and each designated systemically important financial institution to provide to regulators an annual plan for its rapid and orderly resolution in the event of material financial distress or failure (resolution plan). Our resolution plan must, among other things, demonstrate that Goldman Sachs Bank USA (GS Bank USA) is adequately protected from risks arising from our other entities. The regulators' joint rule sets specific standards for the resolution plans, including requiring a detailed resolution strategy and analyses of the company's material entities, organizational structure, interconnections and interdependencies, and management information systems, among other elements. We submitted our resolution plan to the regulators on June 29, 2012. GS Bank USA also submitted its resolution plan on June 29, 2012, as required by the FDIC.

In September 2011, the SEC proposed rules to implement the Dodd-Frank Act's prohibition against securitization participants' engaging in any transaction that would involve or result in any material conflict of interest with an investor in a securitization transaction. The proposed rules would except bona fide market-making activities and risk-mitigating hedging activities in connection with securitization activities from the general prohibition. We will also be affected by rules to be adopted by federal agencies pursuant to the Dodd-Frank Act that require any person who organizes or initiates an asset-backed security transaction to retain a portion (generally, at least five percent) of any credit risk that the person conveys to a third party.

In December 2011, the Federal Reserve Board proposed regulations designed to strengthen the regulation and supervision of large bank holding companies and systemically important nonbank financial institutions. These proposals address, among other things, risk-based capital and leverage requirements, liquidity requirements, overall risk management requirements, single counterparty limits and early remediation requirements that are designed to address financial weakness at an early stage. Although many of the proposals mirror initiatives to which bank holding companies are already subject, their full impact on the firm will not be known with certainty until the rules are finalized and market practices and structures develop under the final rules. In addition, in October 2012, the Federal Reserve Board issued final rules for stress testing requirements for certain bank holding companies, including the firm. See "Equity Capital" below for further information about our Comprehensive Capital Analysis and Review (CCAR).

The Dodd-Frank Act also contains provisions that include (i) requiring the registration of all swap dealers and major swap participants with the CFTC and of security-based swap dealers and major security-based swap participants with the SEC, the clearing and execution of certain swaps and security-based swaps through central counterparties, regulated exchanges or electronic facilities and real-time public and regulatory reporting of trade information, (ii) placing new business conduct standards and other requirements on swap dealers, major swap participants, security-based swap dealers and major security-based swap participants, covering their relationships with counterparties, their internal oversight and compliance structures, conflict of interest rules, internal information barriers, general and trade-specific record-keeping and risk management, (iii) establishing mandatory margin requirements for trades that are not cleared through a central counterparty, (iv) position limits that cap exposure to derivatives on certain physical commodities and (v) entity-level capital requirements for swap dealers, major swap participants, security-based swap dealers and major security-based swap participants.

The CFTC is responsible for issuing rules relating to swaps, swap dealers and major swap participants, and the SEC is responsible for issuing rules relating to security-based swaps, security-based swap dealers and major security-based swap participants. Although the CFTC has not yet finalized its capital regulations, certain of the requirements, including registration of swap dealers and real-time public trade reporting, have taken effect already under CFTC rules, and the SEC and the CFTC have finalized the definitions of a number of key terms. The CFTC has finalized a number of other implementing rules and laid out a series of implementation deadlines in 2013, covering rules for business conduct standards for swap dealers and clearing requirements.

The SEC has proposed rules to impose margin, capital and segregation requirements for security-based swap dealers and major security-based swap participants. The SEC has also proposed rules relating to registration of security-based swap dealers and major security-based swap participants, trade reporting and real-time reporting, and business conduct requirements for security-based swap dealers and major security-based swap participants.

We have registered certain subsidiaries as "swap dealers" under the CFTC rules, including Goldman, Sachs & Co. (GS&Co.), GS Bank USA, Goldman Sachs International (GSI) and J. Aron & Company. We expect that these entities, and our businesses more broadly, will be subject to significant and developing regulation and regulatory oversight in connection with swap-related activities. Similar regulations have been proposed or adopted in jurisdictions outside the United States and, in July 2012 and February 2013, the Basel Committee and the International Organization of Securities Commissions released consultative documents proposing margin requirements for non-centrally-cleared derivatives. The full impact of the various U.S. and non-U.S. regulatory developments in this area will not be known with certainty until the rules are implemented and market practices and structures develop under the final rules.

The Dodd-Frank Act also establishes the Consumer Financial Protection Bureau, which has broad authority to regulate providers of credit, payment and other consumer financial products and services, and has oversight over certain of our products and services.

See Note 20 to the consolidated financial statements for additional information about regulatory developments as they relate to our regulatory capital ratios.

See "Business — Regulation" in Part I, Item 1 of our Annual Report on Form 10-K for more information on the laws, rules and regulations and proposed laws, rules and regulations that apply to us and our operations.

Balance Sheet and Funding Sources

Balance Sheet Management

One of our most important risk management disciplines is our ability to manage the size and composition of our balance sheet. While our asset base changes due to client activity, market fluctuations and business opportunities, the size and composition of our balance sheet reflect (i) our overall risk tolerance, (ii) our ability to access stable funding sources and (iii) the amount of equity capital we hold.

Although our balance sheet fluctuates on a day-to-day basis, our total assets and adjusted assets at quarterly and year-end dates are generally not materially different from those occurring within our reporting periods.

In order to ensure appropriate risk management, we seek to maintain a liquid balance sheet and have processes in place to dynamically manage our assets and liabilities which include:

- quarterly planning;
- business-specific limits;
- monitoring of key metrics; and
- scenario analyses.

Quarterly Planning. We prepare a quarterly balance sheet plan that combines our projected total assets and composition of assets with our expected funding sources and capital levels for the upcoming quarter. The objectives of this quarterly planning process are:

- to develop our near-term balance sheet projections, taking into account the general state of the financial markets and expected business activity levels;
- to ensure that our projected assets are supported by an adequate amount and tenor of funding and that our projected capital and liquidity metrics are within management guidelines and regulatory requirements; and
- to allow business risk managers and managers from our independent control and support functions to objectively evaluate balance sheet limit requests from business managers in the context of the firm's overall balance sheet constraints. These constraints include the firm's liability profile and equity capital levels, maturities and plans for new debt and equity issuances, share repurchases, deposit trends and secured funding transactions.

To prepare our quarterly balance sheet plan, business risk managers and managers from our independent control and support functions meet with business managers to review current and prior period metrics and discuss expectations for the upcoming quarter. The specific metrics reviewed include asset and liability size and composition, aged inventory, limit utilization, risk and performance measures, and capital usage.

Our consolidated quarterly plan, including our balance sheet plans by business, funding and capital projections, and projected capital and liquidity metrics, is reviewed by the Firmwide Finance Committee. See "Overview and Structure of Risk Management" for an overview of our risk management structure.

Business-Specific Limits. The Firmwide Finance Committee sets asset and liability limits for each business and aged inventory limits for certain financial instruments as a disincentive to hold inventory over longer periods of time. These limits are set at levels which are close to actual operating levels in order to ensure prompt escalation and discussion among business managers and managers in our independent control and support functions on a routine basis. The Firmwide Finance Committee reviews and approves balance sheet limits on a quarterly basis and may also approve changes in limits on an ad hoc basis in response to changing business needs or market conditions.

Monitoring of Key Metrics. We monitor key balance sheet metrics daily both by business and on a consolidated basis, including asset and liability size and composition, aged inventory, limit utilization, risk measures and capital usage. We allocate assets to businesses and review and analyze movements resulting from new business activity as well as market fluctuations.

Scenario Analyses. We conduct scenario analyses to determine how we would manage the size and composition of our balance sheet and maintain appropriate funding, liquidity and capital positions in a variety of situations:

- These scenarios cover short-term and long-term time horizons using various macro-economic and firm-specific assumptions. We use these analyses to assist us in developing longer-term funding plans, including the level of unsecured debt issuances, the size of our secured funding program and the amount and composition of our equity capital. We also consider any potential future constraints, such as limits on our ability to grow our asset base in the absence of appropriate funding.
- Through our Internal Capital Adequacy Assessment Process (ICAAP), CCAR, the stress tests we are required to conduct under the Dodd-Frank Act, and our resolution and recovery planning, we further analyze how we would manage our balance sheet and risks through the duration of a severe crisis and we develop plans to access funding, generate liquidity, and/or redeploy or issue equity capital, as appropriate.

Balance Sheet Allocation

In addition to preparing our consolidated statements of financial condition in accordance with U.S. GAAP, we prepare a balance sheet that generally allocates assets to our businesses, which is a non-GAAP presentation and may not be comparable to similar non-GAAP presentations used by other companies. We believe that presenting our assets on this basis is meaningful because it is consistent with the way management views and manages risks associated with the firm's assets and better enables investors to assess the liquidity of the firm's assets. The table below presents a summary of this balance sheet allocation.

	As of December	
in millions	**2012**	2011
Excess liquidity (Global Core Excess)	**$174,622**	$171,581
Other cash	**6,839**	7,888
Excess liquidity and cash	**181,461**	179,469
Secured client financing	**229,442**	283,707
Inventory	**318,323**	273,640
Secured financing agreements	**76,277**	71,103
Receivables	**36,273**	35,769
Institutional Client Services	**430,873**	380,512
ICBC [1]	**2,082**	4,713
Equity (excluding ICBC)	**21,267**	23,041
Debt	**25,386**	23,311
Receivables and other	**8,421**	5,320
Investing & Lending	**57,156**	56,385
Total inventory and related assets	**488,029**	436,897
Other assets [2]	**39,623**	23,152
Total assets	**$938,555**	$923,225

1. In January 2013, we sold approximately 45% of our ordinary shares of ICBC.
2. Includes assets related to our reinsurance business classified as held for sale as of December 2012. See Note 12 to the consolidated financial statements for further information.

The following is a description of the captions in the table above.

Excess Liquidity and Cash. We maintain substantial excess liquidity to meet a broad range of potential cash outflows and collateral needs in the event of a stressed environment. See "Liquidity Risk Management" below for details on the composition and sizing of our excess liquidity pool or "Global Core Excess" (GCE). In addition to our excess liquidity, we maintain other operating cash balances, primarily for use in specific currencies, entities, or jurisdictions where we do not have immediate access to parent company liquidity.

Secured Client Financing. We provide collateralized financing for client positions, including margin loans secured by client collateral, securities borrowed, and resale agreements primarily collateralized by government obligations. As a result of client activities, we are required to segregate cash and securities to satisfy regulatory requirements. Our secured client financing arrangements, which are generally short-term, are accounted for at fair value or at amounts that approximate fair value, and include daily margin requirements to mitigate counterparty credit risk.

Institutional Client Services. In Institutional Client Services, we maintain inventory positions to facilitate market-making in fixed income, equity, currency and commodity products. Additionally, as part of client market-making activities, we enter into resale or securities borrowing arrangements to obtain securities which we can use to cover transactions in which we or our clients have sold securities that have not yet been purchased. The receivables in Institutional Client Services primarily relate to securities transactions.

Investing & Lending. In Investing & Lending, we make investments and originate loans to provide financing to clients. These investments and loans are typically longer-term in nature. We make investments, directly and indirectly through funds that we manage, in debt securities, loans, public and private equity securities, real estate and other investments.

Other Assets. Other assets are generally less liquid, non-financial assets, including property, leasehold improvements and equipment, goodwill and identifiable intangible assets, income tax-related receivables, equity-method investments, assets classified as held for sale and miscellaneous receivables.

The tables below present the reconciliation of this balance sheet allocation to our U.S. GAAP balance sheet. In the tables below, total assets for Institutional Client Services and Investing & Lending represent the inventory and related assets. These amounts differ from total assets by business segment disclosed in Note 25 to the consolidated financial statements because total assets disclosed in Note 25 include allocations of our excess liquidity and cash, secured client financing and other assets.

	As of December 2012					
in millions	**Excess Liquidity and Cash** [1]	**Secured Client Financing**	**Institutional Client Services**	**Investing & Lending**	**Other Assets**	**Total Assets**
Cash and cash equivalents	**$ 72,669**	**$ —**	**$ —**	**$ —**	**$ —**	**$ 72,669**
Cash and securities segregated for regulatory and other purposes	**—**	**49,671**	**—**	**—**	**—**	**49,671**
Securities purchased under agreements to resell and federal funds sold	**28,018**	**84,064**	**28,960**	**292**	**—**	**141,334**
Securities borrowed	**41,699**	**47,877**	**47,317**	**—**	**—**	**136,893**
Receivables from brokers, dealers and clearing organizations	**—**	**4,400**	**14,044**	**36**	**—**	**18,480**
Receivables from customers and counterparties	**—**	**43,430**	**22,229**	**7,215**	**—**	**72,874**
Financial instruments owned, at fair value	**39,075**	**—**	**318,323**	**49,613**	**—**	**407,011**
Other assets	**—**	**—**	**—**	**—**	**39,623**	**39,623**
Total assets	**$181,461**	**$229,442**	**$430,873**	**$57,156**	**$39,623**	**$938,555**

	As of December 2011					
in millions	Excess Liquidity and Cash [1]	Secured Client Financing	Institutional Client Services	Investing & Lending	Other Assets	Total Assets
Cash and cash equivalents	$ 56,008	$ —	$ —	$ —	$ —	$ 56,008
Cash and securities segregated for regulatory and other purposes	—	64,264	—	—	—	64,264
Securities purchased under agreements to resell and federal funds sold	70,220	98,445	18,671	453	—	187,789
Securities borrowed	14,919	85,990	52,432	—	—	153,341
Receivables from brokers, dealers and clearing organizations	—	3,252	10,612	340	—	14,204
Receivables from customers and counterparties	—	31,756	25,157	3,348	—	60,261
Financial instruments owned, at fair value	38,322	—	273,640	52,244	—	364,206
Other assets	—	—	—	—	23,152	23,152
Total assets	$179,469	$283,707	$380,512	$56,385	$23,152	$923,225

1. Includes unencumbered cash, U.S. government and federal agency obligations (including highly liquid U.S. federal agency mortgage-backed obligations), and German, French, Japanese and United Kingdom government obligations.

Balance Sheet Analysis and Metrics

As of December 2012, total assets on our consolidated statements of financial condition were $938.56 billion, an increase of $15.33 billion from December 2011. This increase was primarily due to (i) an increase in financial instruments owned, at fair value of $42.81 billion, due to increases in equities and convertible debentures and non-U.S. government and agency obligations and (ii) an increase in cash and cash equivalents of $16.66 billion, primarily due to increases in interest-bearing deposits with banks. These increases were partially offset by decreases in securities purchased under agreements to resell and federal funds sold of $46.46 billion, primarily due to firm and client activities.

As of December 2012, total liabilities on our consolidated statements of financial condition were $862.84 billion, an increase of $9.99 billion from December 2011. This increase was primarily due to an increase in deposits of $24.02 billion, primarily due to increases in client activity. This increase was partially offset by a decrease in financial instruments sold, but not yet purchased, at fair value of $18.37 billion, primarily due to decreases in derivatives and U.S. government and federal agency obligations.

As of December 2012, our total securities sold under agreements to repurchase, accounted for as collateralized financings, were $171.81 billion, which was essentially unchanged and 3% higher than the daily average amount of repurchase agreements during the quarter ended and year ended December 2012, respectively. As of December 2012, the increase in our repurchase agreements relative to the daily average during the year was primarily due to an increase in firm financing activities. As of December 2011, our total securities sold under agreements to repurchase, accounted for as collateralized financings, were $164.50 billion, which was 7% higher and 3% higher than the daily average amount of repurchase agreements during the quarter ended and year ended December 2011, respectively. As of December 2011, the increase in our repurchase agreements relative to the daily average during the quarter and year was primarily due to increases in client activity at the end of the year. The level of our repurchase agreements fluctuates between and within periods, primarily due to providing clients with access to highly liquid collateral, such as U.S. government and federal agency, and investment-grade sovereign obligations through collateralized financing activities.

The table below presents information on our assets, unsecured long-term borrowings, shareholders' equity and leverage ratios.

	As of December	
$ in millions	**2012**	2011
Total assets	**$938,555**	$923,225
Adjusted assets	**$686,874**	$604,391
Unsecured long-term borrowings	**$167,305**	$173,545
Total shareholders' equity	**$ 75,716**	$ 70,379
Leverage ratio	**12.4x**	13.1x
Adjusted leverage ratio	**9.1x**	8.6x
Debt to equity ratio	**2.2x**	2.5x

Adjusted assets. Adjusted assets equals total assets less (i) low-risk collateralized assets generally associated with our secured client financing transactions, federal funds sold and excess liquidity (which includes financial instruments sold, but not yet purchased, at fair value, less derivative liabilities) and (ii) cash and securities we segregate for regulatory and other purposes. Adjusted assets is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies.

The table below presents the reconciliation of total assets to adjusted assets.

		As of December	
in millions		**2012**	2011
Total assets		**$ 938,555**	$ 923,225
Deduct:	Securities borrowed	**(136,893)**	(153,341)
	Securities purchased under agreements to resell and federal funds sold	**(141,334)**	(187,789)
Add:	Financial instruments sold, but not yet purchased, at fair value	**126,644**	145,013
	Less derivative liabilities	**(50,427)**	(58,453)
	Subtotal	**(202,010)**	(254,570)
Deduct:	Cash and securities segregated for regulatory and other purposes	**(49,671)**	(64,264)
Adjusted assets		**$ 686,874**	$ 604,391

Leverage ratio. The leverage ratio equals total assets divided by total shareholders' equity and measures the proportion of equity and debt the firm is using to finance assets. This ratio is different from the Tier 1 leverage ratio included in "Equity Capital — Consolidated Regulatory Capital Ratios" below, and further described in Note 20 to the consolidated financial statements.

Adjusted leverage ratio. The adjusted leverage ratio equals adjusted assets divided by total shareholders' equity. We believe that the adjusted leverage ratio is a more meaningful measure of our capital adequacy than the leverage ratio because it excludes certain low-risk collateralized assets that are generally supported with little or no capital. The adjusted leverage ratio is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies.

Our adjusted leverage ratio increased to 9.1x as of December 2012 from 8.6x as of December 2011 as our adjusted assets increased.

Debt to equity ratio. The debt to equity ratio equals unsecured long-term borrowings divided by total shareholders' equity.

Funding Sources

Our primary sources of funding are secured financings, unsecured long-term and short-term borrowings, and deposits. We seek to maintain broad and diversified funding sources globally.

We raise funding through a number of different products, including:

- collateralized financings, such as repurchase agreements, securities loaned and other secured financings;
- long-term unsecured debt (including structured notes) through syndicated U.S. registered offerings, U.S. registered and 144A medium-term note programs, offshore medium-term note offerings and other debt offerings;
- savings and demand deposits through deposit sweep programs and time deposits through internal and third-party broker-dealers; and
- short-term unsecured debt through U.S. and non-U.S. commercial paper and promissory note issuances and other methods.

We generally distribute our funding products through our own sales force and third-party distributors, to a large, diverse creditor base in a variety of markets in the Americas, Europe and Asia. We believe that our relationships with our creditors are critical to our liquidity. Our creditors include banks, governments, securities lenders, pension funds, insurance companies, mutual funds and individuals. We have imposed various internal guidelines to monitor creditor concentration across our funding programs.

Secured Funding. We fund a significant amount of inventory on a secured basis. Secured funding is less sensitive to changes in our credit quality than unsecured funding, due to our posting of collateral to our lenders. Nonetheless, we continually analyze the refinancing risk of our secured funding activities, taking into account trade tenors, maturity profiles, counterparty concentrations, collateral eligibility and counterparty rollover probabilities. We seek to mitigate our refinancing risk by executing term trades with staggered maturities, diversifying counterparties, raising excess secured funding, and pre-funding residual risk through our GCE.

We seek to raise secured funding with a term appropriate for the liquidity of the assets that are being financed, and we seek longer maturities for secured funding collateralized by asset classes that may be harder to fund on a secured basis especially during times of market stress. Substantially all of our secured funding is executed for tenors of one month or greater. Assets that may be harder to fund on a secured basis during times of market stress include certain financial instruments in the following categories: mortgage and other asset-backed loans and securities, non-investment grade corporate debt securities, equities and convertible debentures and emerging market securities. Assets that are classified as level 3 in the fair value hierarchy are generally funded on an unsecured basis. See Note 6 to the consolidated financial statements for further information about the classification of financial instruments in the fair value hierarchy and see "—Unsecured Long-Term Borrowings" below for further information about the use of unsecured long-term borrowings as a source of funding.

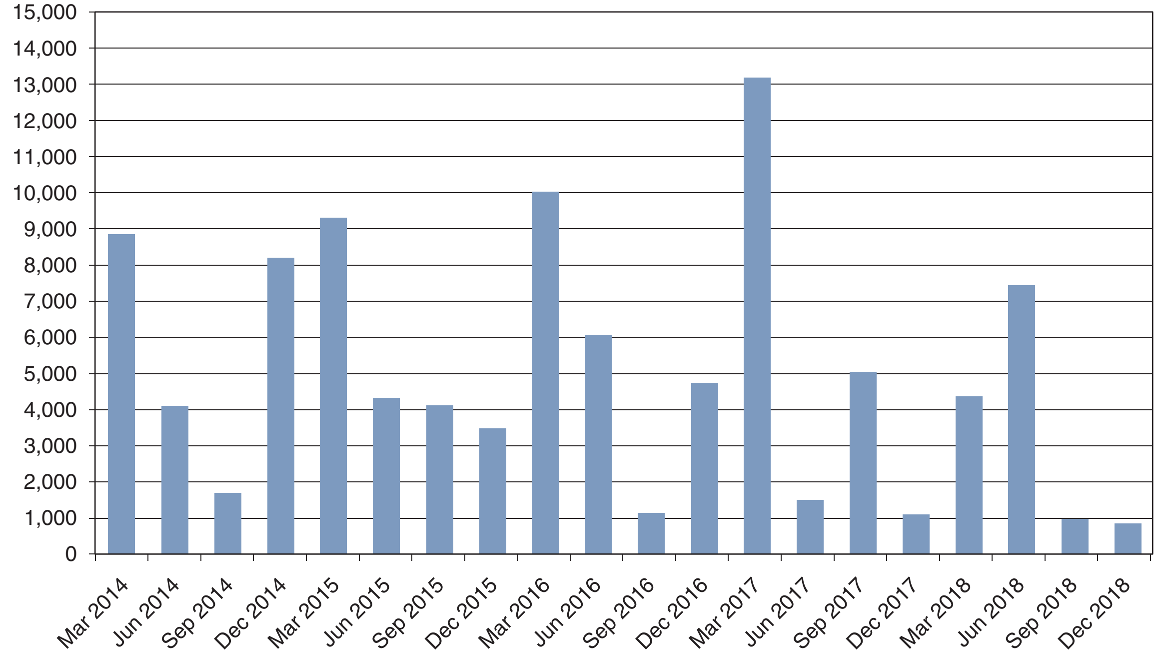
The weighted average maturity of our secured funding, excluding funding collateralized by highly liquid securities eligible for inclusion in our GCE, exceeded 100 days as of December 2012.

A majority of our secured funding for securities not eligible for inclusion in the GCE is executed through term repurchase agreements and securities lending contracts. We also raise financing through other types of collateralized financings, such as secured loans and notes.

GS Bank USA has access to funding through the Federal Reserve Bank discount window. While we do not rely on this funding in our liquidity planning and stress testing, we maintain policies and procedures necessary to access this funding and test discount window borrowing procedures.

Unsecured Long-Term Borrowings. We issue unsecured long-term borrowings as a source of funding for inventory and other assets and to finance a portion of our GCE. We issue in different tenors, currencies, and products to maximize the diversification of our investor base. The table below presents our quarterly unsecured long-term borrowings maturity profile through 2018 as of December 2012.

Unsecured Long-Term Borrowings Maturity Profile
$ in millions



The weighted average maturity of our unsecured long-term borrowings as of December 2012 was approximately eight years. To mitigate refinancing risk, we seek to limit the principal amount of debt maturing on any one day or during any week or year. We enter into interest rate swaps to convert a substantial portion of our long-term borrowings into floating-rate obligations in order to manage our exposure to interest rates. See Note 16 to the consolidated financial statements for further information about our unsecured long-term borrowings.

Temporary Liquidity Guarantee Program (TLGP). The remaining portion of our senior unsecured short-term debt guaranteed by the FDIC under the TLGP matured during the second quarter of 2012. As of December 2012, no borrowings guaranteed by the FDIC under the TLGP were outstanding and the program had expired for new issuances.

Deposits. As part of our efforts to diversify our funding base, deposits have become a more meaningful share of our funding activities. GS Bank USA has been actively growing its deposit base with an emphasis on issuance of long-term certificates of deposit and on expanding our deposit sweep program, which involves long-term contractual agreements with several U.S. broker-dealers who sweep client cash to FDIC-insured deposits. We utilize deposits to finance activities in our bank subsidiaries. The table below presents the sourcing of our deposits.

	As of December 2012	
	Type of Deposit	
in millions	Savings and Demand [1]	Time [2]
Private bank deposits [3]	$30,460	$ —
Certificates of deposit	—	21,507
Deposit sweep programs	15,998	—
Institutional	51	2,108
Total [4]	**$46,509**	**$23,615**

1. Represents deposits with no stated maturity.
2. Weighted average maturity in excess of three years.
3. Substantially all were from overnight deposit sweep programs related to private wealth management clients.
4. Deposits insured by the FDIC as of December 2012 were approximately $42.77 billion.

Unsecured Short-Term Borrowings. A significant portion of our short-term borrowings was originally long-term debt that is scheduled to mature within one year of the reporting date. We use short-term borrowings to finance liquid assets and for other cash management purposes. We primarily issue commercial paper, promissory notes, and other hybrid instruments.

As of December 2012, our unsecured short-term borrowings, including the current portion of unsecured long-term borrowings, were $44.30 billion. See Note 15 to the consolidated financial statements for further information about our unsecured short-term borrowings.

Equity Capital

Capital adequacy is of critical importance to us. Our objective is to be conservatively capitalized in terms of the amount and composition of our equity base. Accordingly, we have in place a comprehensive capital management policy that serves as a guide to determine the amount and composition of equity capital we maintain.

The level and composition of our equity capital are determined by multiple factors including our current and future consolidated regulatory capital requirements, our ICAAP, CCAR and results of stress tests, and may also be influenced by other factors such as rating agency guidelines, subsidiary capital requirements, the business environment, conditions in the financial markets and assessments of potential future losses due to adverse changes in our business and market environments. In addition, we maintain a capital plan which projects sources and uses of capital given a range of business environments, and a contingency capital plan which provides a framework for analyzing and responding to an actual or perceived capital shortfall.

As part of the Federal Reserve Board's annual CCAR, U.S. bank holding companies with total consolidated assets of $50 billion or greater are required to submit annual capital plans for review by the Federal Reserve Board. The purpose of the Federal Reserve Board's review is to ensure that these institutions have robust, forward-looking capital planning processes that account for their unique risks and that permit continued operations during times of economic and financial stress. The Federal Reserve Board will evaluate a bank holding company based on whether it has the capital necessary to continue operating under the baseline and stressed scenarios provided by the Federal Reserve. As part of the capital plan review, the Federal Reserve Board evaluates an institution's plan to make capital distributions, such as increasing dividend payments or repurchasing or redeeming stock, across a range of macro-economic and firm-specific assumptions. In addition, the rules adopted by the Federal Reserve Board under the Dodd-Frank Act, require us to conduct stress tests on a semi-annual basis and publish a summary of certain results, beginning in March 2013. The Federal Reserve Board will conduct its own annual stress tests and is expected to publish a summary of certain results in March 2013.

As part of our 2012 CCAR submission, the Federal Reserve informed us that it did not object to our proposed capital actions through the first quarter of 2013, including the repurchase of outstanding common stock and increases in the quarterly common stock dividend. We submitted our 2013 CCAR to the Federal Reserve on January 7, 2013 and expect to publish a summary of our results in March 2013.

Our consolidated regulatory capital requirements are determined by the Federal Reserve Board, as described below. Our ICAAP incorporates an internal risk-based capital assessment designed to identify and measure material risks associated with our business activities, including market risk, credit risk and operational risk, in a manner that is closely aligned with our risk management practices. Our internal risk-based capital assessment is supplemented with the results of stress tests.

As of December 2012, our total shareholders' equity was $75.72 billion (consisting of common shareholders' equity of $69.52 billion and preferred stock of $6.20 billion). As of December 2011, our total shareholders' equity was $70.38 billion (consisting of common shareholders' equity of $67.28 billion and preferred stock of $3.10 billion). In addition, as of December 2012 and December 2011, $2.73 billion and $5.00 billion, respectively, of our junior subordinated debt issued to trusts qualified as equity capital for regulatory and certain rating agency purposes. See "— Consolidated Regulatory Capital Ratios" below for information regarding the impact of regulatory developments.

Consolidated Regulatory Capital

The Federal Reserve Board is the primary regulator of Group Inc., a bank holding company under the Bank Holding Company Act of 1956 (BHC Act) and a financial holding company under amendments to the BHC Act effected by the U.S. Gramm-Leach-Bliley Act of 1999. As a bank holding company, we are subject to consolidated regulatory capital requirements that are computed in accordance with the Federal Reserve Board's risk-based capital requirements (which are based on the 'Basel 1' Capital Accord of the Basel Committee). These capital requirements are expressed as capital ratios that compare measures of capital to risk-weighted assets (RWAs). See Note 20 to the consolidated financial statements for additional information regarding the firm's RWAs. The firm's capital levels are also subject to qualitative judgments by its regulators about components, risk weightings and other factors.

Federal Reserve Board regulations require bank holding companies to maintain a minimum Tier 1 capital ratio of 4% and a minimum total capital ratio of 8%. The required minimum Tier 1 capital ratio and total capital ratio in order to be considered a "well-capitalized" bank holding company under the Federal Reserve Board guidelines are 6% and 10%, respectively. Bank holding companies may be expected to maintain ratios well above the minimum levels, depending on their particular condition, risk profile and growth plans. The minimum Tier 1 leverage ratio is 3% for bank holding companies that have received the highest supervisory rating under Federal Reserve Board guidelines or that have implemented the Federal Reserve Board's risk-based capital measure for market risk. Other bank holding companies must have a minimum Tier 1 leverage ratio of 4%.

Consolidated Regulatory Capital Ratios

The table below presents information about our regulatory capital ratios, which are based on Basel 1, as implemented by the Federal Reserve Board.

	As of December	
$ in millions	**2012**	2011
Common shareholders' equity	**$ 69,516**	$ 67,279
Less: Goodwill	**(3,702)**	(3,802)
Less: Intangible assets	**(1,397)**	(1,666)
Less: Equity investments in certain entities [1]	**(4,805)**	(4,556)
Less: Disallowed deferred tax assets	**(1,261)**	(1,073)
Less: Debt valuation adjustment [2]	**(180)**	(664)
Less: Other adjustments [3]	**(124)**	(356)
Tier 1 Common Capital	**58,047**	55,162
Non-cumulative preferred stock	**6,200**	3,100
Junior subordinated debt issued to trusts [4]	**2,730**	5,000
Tier 1 Capital	**66,977**	63,262
Qualifying subordinated debt [5]	**13,342**	13,828
Other adjustments	**87**	53
Tier 2 Capital	**13,429**	13,881
Total Capital	**$ 80,406**	$ 77,143
Risk-Weighted Assets	**$399,928**	$457,027
Tier 1 Capital Ratio	**16.7%**	13.8%
Total Capital Ratio	**20.1%**	16.9%
Tier 1 Leverage Ratio [6]	**7.3%**	7.0%
Tier 1 Common Ratio [7]	**14.5%**	12.1%

1. Primarily represents a portion of our equity investments in non-financial companies.
2. Represents the cumulative change in the fair value of our unsecured borrowings attributable to the impact of changes in our own credit spreads (net of tax at the applicable tax rate).
3. Includes net unrealized gains/(losses) on available-for-sale securities (net of tax at the applicable tax rate), the cumulative change in our pension and postretirement liabilities (net of tax at the applicable tax rate) and investments in certain nonconsolidated entities.
4. See Note 16 to the consolidated financial statements for additional information about the junior subordinated debt issued to trusts.
5. Substantially all of our subordinated debt qualifies as Tier 2 capital for Basel 1 purposes.
6. See Note 20 to the consolidated financial statements for additional information about the firm's Tier 1 leverage ratio.
7. The Tier 1 common ratio equals Tier 1 common capital divided by RWAs. We believe that the Tier 1 common ratio is meaningful because it is one of the measures that we and investors use to assess capital adequacy and, while not currently a formal regulatory capital ratio, this measure is of increasing importance to regulators. The Tier 1 common ratio is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies.

Our Tier 1 capital ratio increased to 16.7% as of December 2012 from 13.8% as of December 2011 primarily reflecting an increase in common shareholders' equity and a reduction in market RWAs. The reduction in market RWAs was primarily driven by lower volatilities, a decrease in derivative exposure and capital efficiency initiatives that, while driven by future Basel 3 rules, also reduced market RWAs as measured under the current rules.

Changes to the market risk capital rules of the U.S. federal bank regulatory agencies became effective on January 1, 2013. These changes require the addition of several new model-based capital requirements, as well as an increase in capital requirements for securitization positions, and are designed to implement the new market risk framework of the Basel Committee, as well as the prohibition on the use of external credit ratings, as required by the Dodd-Frank Act. This revised market risk framework is a significant part of the regulatory capital changes that will ultimately be included in our Basel 3 capital ratios. The firm's estimated Tier 1 common ratio under Basel 1 reflecting these revised market risk regulatory capital requirements would have been approximately 350 basis points lower than the firm's reported Basel 1 Tier 1 common ratio as of December 2012.

See "Business — Regulation" in Part I, Item 1 of our Annual Report on Form 10-K and Note 20 to the consolidated financial statements for additional information about our regulatory capital ratios and the related regulatory requirements, including pending and proposed regulatory changes.

Risk-Weighted Assets

RWAs under the Federal Reserve Board's risk-based capital requirements are calculated based on the amount of credit risk and market risk.

RWAs for credit risk reflect amounts for on-balance sheet and off–balance sheet exposures. Credit risk requirements for on-balance sheet assets, such as receivables and cash, are generally based on the balance sheet value. Credit risk requirements for securities financing transactions are determined based upon the positive net exposure for each trade, and include the effect of counterparty netting and collateral, as applicable. For off-balance sheet exposures, including commitments and guarantees, a credit equivalent amount is calculated based on the notional amount of each trade. Requirements for OTC derivatives are based on a combination of positive net exposure and a percentage of the notional amount of each trade, and include the effect of counterparty netting and collateral, as applicable. All such assets and exposures are then assigned a risk weight depending on, among other things, whether the counterparty is a sovereign, bank or a qualifying securities firm or other entity (or if collateral is held, depending on the nature of the collateral).

RWAs for market risk are comprised of modeled and non-modeled risk requirements. Modeled risk requirements are determined by reference to the firm's Value-at-Risk (VaR) model. VaR is the potential loss in value of inventory positions due to adverse market movements over a defined time horizon with a specified confidence level. We use a single VaR model which captures risks including interest rates, equity prices, currency rates and commodity prices. For certain portfolios of debt and equity positions, the modeled RWAs also reflect requirements for specific risk, which is the risk of loss on a position that could result from changes in risk factors unique to that position. Regulatory VaR used for capital requirements will differ from risk management VaR, due to different time horizons (10-day vs. 1-day), confidence levels (99% vs. 95%), as well as other factors. Non-modeled risk requirements reflect specific risk for other debt and equity positions. The standardized measurement method is used to determine non-modeled risk by applying supervisory defined risk-weighting factors to positions after applicable netting is performed.

The table below presents information on the components of RWAs within our consolidated regulatory capital ratios.

	As of December	
in millions	**2012**	2011
Credit RWAs		
OTC derivatives	**$107,269**	$119,848
Commitments and guarantees [1]	**46,007**	37,648
Securities financing transactions [2]	**47,069**	53,236
Other [3]	**87,181**	84,039
Total Credit RWAs	**$287,526**	$294,771
Market RWAs		
Modeled requirements	**$ 23,302**	$ 57,784
Non-modeled requirements	**89,100**	104,472
Total Market RWAs	**112,402**	162,256
Total RWAs [4]	**$399,928**	$457,027

1. Principally includes certain commitments to extend credit and letters of credit.
2. Represents resale and repurchase agreements and securities borrowed and loaned transactions.
3. Principally includes receivables from customers, other assets, cash and cash equivalents and available-for-sale securities.
4. Under the current regulatory capital framework, there is no explicit requirement for Operational Risk.

As outlined above, changes to the market risk capital rules that became effective on January 1, 2013, require the addition of several new model-based capital requirements, as well as an increase in capital requirements for securitization positions.

Internal Capital Adequacy Assessment Process

We perform an ICAAP with the objective of ensuring that the firm is appropriately capitalized relative to the risks in our business.

As part of our ICAAP, we perform an internal risk-based capital assessment. This assessment incorporates market risk, credit risk and operational risk. Market risk is calculated by using VaR calculations supplemented by risk-based add-ons which include risks related to rare events (tail risks). Credit risk utilizes assumptions about our counterparties' probability of default, the size of our losses in the event of a default and the maturity of our counterparties' contractual obligations to us. Operational risk is calculated based on scenarios incorporating multiple types of operational failures. Backtesting is used to gauge the effectiveness of models at capturing and measuring relevant risks.

We evaluate capital adequacy based on the result of our internal risk-based capital assessment, supplemented with the results of stress tests which measure the firm's estimated performance under various market conditions. Our goal is to hold sufficient capital, under our internal risk-based capital framework, to ensure we remain adequately capitalized after experiencing a severe stress event. Our assessment of capital adequacy is viewed in tandem with our assessment of liquidity adequacy and is integrated into the overall risk management structure, governance and policy framework of the firm.

We attribute capital usage to each of our businesses based upon our internal risk-based capital and regulatory frameworks and manage the levels of usage based upon the balance sheet and risk limits established.

Rating Agency Guidelines

The credit rating agencies assign credit ratings to the obligations of Group Inc., which directly issues or guarantees substantially all of the firm's senior unsecured obligations. GS&Co. and GSI have been assigned long- and short-term issuer ratings by certain credit rating agencies. GS Bank USA has also been assigned long-term issuer ratings as well as ratings on its long-term and short-term bank deposits. In addition, credit rating agencies have assigned ratings to debt obligations of certain other subsidiaries of Group Inc.

The level and composition of our equity capital are among the many factors considered in determining our credit ratings. Each agency has its own definition of eligible capital and methodology for evaluating capital adequacy, and assessments are generally based on a combination of factors rather than a single calculation. See "Liquidity Risk Management — Credit Ratings" for further information about credit ratings of Group Inc., GS&Co., GSI and GS Bank USA.

Subsidiary Capital Requirements

Many of our subsidiaries, including GS Bank USA and our broker-dealer subsidiaries, are subject to separate regulation and capital requirements of the jurisdictions in which they operate.

GS Bank USA is subject to minimum capital requirements that are calculated in a manner similar to those applicable to bank holding companies and computes its capital ratios in accordance with the regulatory capital requirements currently applicable to state member banks, which are based on Basel 1, as implemented by the Federal Reserve Board. As of December 2012, GS Bank USA's Tier 1 Capital ratio under Basel 1 as implemented by the Federal Reserve Board was 18.9%. See Note 20 to the consolidated financial statements for further information about GS Bank USA's regulatory capital ratios under Basel 1, as implemented by the Federal Reserve Board. Effective January 1, 2013, GS Bank USA also implemented the revised market risk framework outlined above. This revised market risk framework is a significant part of the regulatory capital changes that will ultimately be included in GS Bank USA's Basel 3 capital ratios.

For purposes of assessing the adequacy of its capital, GS Bank USA has established an ICAAP which is similar to that used by Group Inc. In addition, the rules adopted by the Federal Reserve Board under the Dodd-Frank Act require GS Bank USA to conduct stress tests on an annual basis and publish a summary of certain results, beginning in March 2013. GS Bank USA submitted its annual stress results to the Federal Reserve on January 7, 2013 and expects to publish a summary of its results in March 2013. GS Bank USA's capital levels and prompt corrective action classification are subject to qualitative judgments by its regulators about components, risk weightings and other factors.

We expect that the capital requirements of several of our subsidiaries are likely to increase in the future due to the various developments arising from the Basel Committee, the Dodd-Frank Act, and other governmental entities and regulators. See Note 20 to the consolidated financial statements for information about the capital requirements of our other regulated subsidiaries and the potential impact of regulatory reform.

Subsidiaries not subject to separate regulatory capital requirements may hold capital to satisfy local tax and legal guidelines, rating agency requirements (for entities with assigned credit ratings) or internal policies, including policies concerning the minimum amount of capital a subsidiary should hold based on its underlying level of risk. In certain instances, Group Inc. may be limited in its ability to access capital held at certain subsidiaries as a result of regulatory, tax or other constraints. As of December 2012 and December 2011, Group Inc.'s equity investment in subsidiaries was $73.32 billion and $67.70 billion, respectively, compared with its total shareholders' equity of $75.72 billion and $70.38 billion, respectively.

Group Inc. has guaranteed the payment obligations of GS&Co., GS Bank USA, and Goldman Sachs Execution & Clearing, L.P. (GSEC) subject to certain exceptions. In November 2008, Group Inc. contributed subsidiaries into GS Bank USA, and Group Inc. agreed to guarantee certain losses, including credit-related losses, relating to assets held by the contributed entities. In connection with this guarantee, Group Inc. also agreed to pledge to GS Bank USA certain collateral, including interests in subsidiaries and other illiquid assets.

Our capital invested in non-U.S. subsidiaries is generally exposed to foreign exchange risk, substantially all of which is managed through a combination of derivatives and non-U.S. denominated debt.

Contingency Capital Plan

Our contingency capital plan provides a framework for analyzing and responding to a perceived or actual capital deficiency, including, but not limited to, identification of drivers of a capital deficiency, as well as mitigants and potential actions. It outlines the appropriate communication procedures to follow during a crisis period, including internal dissemination of information as well as ensuring timely communication with external stakeholders.

Equity Capital Management

Our objective is to maintain a sufficient level and optimal composition of equity capital. We principally manage our capital through issuances and repurchases of our common stock. We may also, from time to time, issue or repurchase our preferred stock, junior subordinated debt issued to trusts and other subordinated debt or other forms of capital as business conditions warrant and subject to approval of the Federal Reserve Board. We manage our capital requirements principally by setting limits on balance sheet assets and/or limits on risk, in each case both at the consolidated and business levels. We attribute capital usage to each of our businesses based upon our internal risk-based capital and regulatory frameworks and manage the levels of usage based upon the balance sheet and risk limits established.

See Notes 16 and 19 to the consolidated financial statements for further information about our preferred stock, junior subordinated debt issued to trusts and other subordinated debt.

Berkshire Hathaway Warrant. In October 2008, we issued Berkshire Hathaway a warrant, which grants Berkshire Hathaway the option to purchase up to 43.5 million shares of common stock at an exercise price of $115.00 per share on or before October 1, 2013. See Note 19 to the consolidated financial statements for information about the Series G Preferred Stock.

Share Repurchase Program. We seek to use our share repurchase program to help maintain the appropriate level of common equity. The repurchase program is effected primarily through regular open-market purchases, the amounts and timing of which are determined primarily by our current and projected capital positions (i.e., comparisons of our desired level and composition of capital to our actual level and composition of capital), but which may also be influenced by general market conditions and the prevailing price and trading volumes of our common stock.

As of December 2012, under the share repurchase program approved by the Board of Directors of Group Inc. (Board), we can repurchase up to 21.5 million additional shares of common stock; however, any such repurchases are subject to the approval of the Federal Reserve Board. See "Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities" in Part II, Item 5 of our Annual Report on Form 10-K and Note 19 to the consolidated financial statements for additional information on our repurchase program and see above for information about the annual CCAR.

Other Capital Metrics

The table below presents information on our shareholders' equity and book value per common share.

	As of December	
in millions, except per share amounts	**2012**	2011
Total shareholders' equity	**$75,716**	$70,379
Common shareholders' equity	**69,516**	67,279
Tangible common shareholders' equity	**64,417**	61,811
Book value per common share	**144.67**	130.31
Tangible book value per common share	**134.06**	119.72

Tangible common shareholders' equity. Tangible common shareholders' equity equals total shareholders' equity less preferred stock, goodwill and identifiable intangible assets. We believe that tangible common shareholders' equity is meaningful because it is a measure that we and investors use to assess capital adequacy. Tangible common shareholders' equity is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies.

The table below presents the reconciliation of total shareholders' equity to tangible common shareholders' equity.

	As of December	
in millions	**2012**	2011
Total shareholders' equity	**$75,716**	$70,379
Deduct: Preferred stock	**(6,200)**	(3,100)
Common shareholders' equity	**69,516**	67,279
Deduct: Goodwill and identifiable intangible assets	**(5,099)**	(5,468)
Tangible common shareholders' equity	**$64,417**	$61,811

Book value and tangible book value per common share. Book value and tangible book value per common share are based on common shares outstanding, including restricted stock units granted to employees with no future service requirements, of 480.5 million and 516.3 million as of December 2012 and December 2011, respectively. We believe that tangible book value per common share (tangible common shareholders' equity divided by common shares outstanding) is meaningful because it is a measure that we and investors use to assess capital adequacy. Tangible book value per common share is a non-GAAP measure and may not be comparable to similar non-GAAP measures used by other companies.

Off-Balance-Sheet Arrangements and Contractual Obligations

Off-Balance-Sheet Arrangements

We have various types of off-balance-sheet arrangements that we enter into in the ordinary course of business. Our involvement in these arrangements can take many different forms, including:

- purchasing or retaining residual and other interests in special purpose entities such as mortgage-backed and other asset-backed securitization vehicles;
- holding senior and subordinated debt, interests in limited and general partnerships, and preferred and common stock in other nonconsolidated vehicles;
- entering into interest rate, foreign currency, equity, commodity and credit derivatives, including total return swaps;
- entering into operating leases; and
- providing guarantees, indemnifications, loan commitments, letters of credit and representations and warranties.

We enter into these arrangements for a variety of business purposes, including securitizations. The securitization vehicles that purchase mortgages, corporate bonds, and other types of financial assets are critical to the functioning of several significant investor markets, including the mortgage-backed and other asset-backed securities markets, since they offer investors access to specific cash flows and risks created through the securitization process.

We also enter into these arrangements to underwrite client securitization transactions; provide secondary market liquidity; make investments in performing and nonperforming debt, equity, real estate and other assets; provide investors with credit-linked and asset-repackaged notes; and receive or provide letters of credit to satisfy margin requirements and to facilitate the clearance and settlement process.

Our financial interests in, and derivative transactions with, such nonconsolidated entities are generally accounted for at fair value, in the same manner as our other financial instruments, except in cases where we apply the equity method of accounting.

The table below presents where a discussion of our various off-balance-sheet arrangements may be found in this Annual Report. In addition, see Note 3 to the consolidated financial statements for a discussion of our consolidation policies.

Type of Off-Balance-Sheet Arrangement	Disclosure in Annual Report
Variable interests and other obligations, including contingent obligations, arising from variable interests in nonconsolidated VIEs	See Note 11 to the consolidated financial statements.
Leases, letters of credit, and lending and other commitments	See "Contractual Obligations" below and Note 18 to the consolidated financial statements.
Guarantees	See "Contractual Obligations" below and Note 18 to the consolidated financial statements.
Derivatives	See Notes 4, 5, 7 and 18 to the consolidated financial statements.

Contractual Obligations

We have certain contractual obligations which require us to make future cash payments. These contractual obligations include our unsecured long-term borrowings, secured long-term financings, time deposits, contractual interest payments and insurance agreements, all of which are included in our consolidated statements of financial condition. Our obligations to make future cash payments also include certain off-balance-sheet contractual obligations such as purchase obligations, minimum rental payments under noncancelable leases and commitments and guarantees.

The table below presents our contractual obligations, commitments and guarantees as of December 2012.

in millions	2013	2014-2015	2016-2017	2018-Thereafter	Total
Amounts related to on-balance-sheet obligations					
Time deposits [1]	$ —	$ 7,151	$ 4,064	$ 5,069	$ 16,284
Secured long-term financings [2]	—	6,403	1,140	1,422	8,965
Unsecured long-term borrowings [3]	—	43,920	42,601	80,784	167,305
Contractual interest payments [4]	7,489	13,518	10,182	33,332	64,521
Insurance liabilities [5]	477	959	934	13,740	16,110
Subordinated liabilities issued by consolidated VIEs	59	62	84	1,155	1,360
Amounts related to off-balance-sheet arrangements					
Commitments to extend credit	10,435	16,322	43,453	5,412	75,622
Contingent and forward starting resale and securities borrowing agreements	47,599	—	—	—	47,599
Forward starting repurchase and secured lending agreements	6,144	—	—	—	6,144
Letters of credit	614	160	—	15	789
Investment commitments	1,378	2,174	258	3,529	7,339
Other commitments	4,471	53	31	69	4,624
Minimum rental payments	439	752	623	1,375	3,189
Derivative guarantees	339,460	213,012	49,413	61,264	663,149
Securities lending indemnifications	27,123	—	—	—	27,123
Other financial guarantees	904	442	1,195	938	3,479

1. Excludes $7.33 billion of time deposits maturing within one year.
2. The aggregate contractual principal amount of secured long-term financings for which the fair value option was elected, primarily consisting of transfers of financial assets accounted for as financings rather than sales and certain other nonrecourse financings, exceeded their related fair value by $115 million.
3. Includes $10.51 billion related to interest rate hedges on certain unsecured long-term borrowings. In addition, the fair value of unsecured long-term borrowings (principal and non-principal-protected) for which the fair value option was elected exceeded the related aggregate contractual principal amount by $379 million. Excludes $77 million of unsecured long-term borrowings related to our reinsurance business classified as held for sale as of December 2012. See Note 17 to the consolidated financial statements for further information.
4. Represents estimated future interest payments related to unsecured long-term borrowings, secured long-term financings and time deposits based on applicable interest rates as of December 2012. Includes stated coupons, if any, on structured notes.
5. Represents estimated undiscounted payments related to future benefits and unpaid claims arising from policies associated with our insurance activities, excluding separate accounts and estimated recoveries under reinsurance contracts. Excludes $13.08 billion of insurance liabilities related to our reinsurance business classified as held for sale as of December 2012. See Note 17 to the consolidated financial statements for further information.

In the table above:

- Obligations maturing within one year of our financial statement date or redeemable within one year of our financial statement date at the option of the holder are excluded and are treated as short-term obligations.
- Obligations that are repayable prior to maturity at our option are reflected at their contractual maturity dates and obligations that are redeemable prior to maturity at the option of the holders are reflected at the dates such options become exercisable.
- Amounts included in the table do not necessarily reflect the actual future cash flow requirements for these arrangements because commitments and guarantees represent notional amounts and may expire unused or be reduced or cancelled at the counterparty's request.
- Due to the uncertainty of the timing and amounts that will ultimately be paid, our liability for unrecognized tax benefits has been excluded. See Note 24 to the consolidated financial statements for further information about our unrecognized tax benefits.

See Notes 15 and 18 to the consolidated financial statements for further information about our short-term borrowings, and commitments and guarantees.

As of December 2012, our unsecured long-term borrowings were $167.31 billion, with maturities extending to 2061, and consisted principally of senior borrowings. See Note 16 to the consolidated financial statements for further information about our unsecured long-term borrowings.

As of December 2012, our future minimum rental payments net of minimum sublease rentals under noncancelable leases were $3.19 billion. These lease commitments, principally for office space, expire on various dates through 2069. Certain agreements are subject to periodic escalation provisions for increases in real estate taxes and other charges. See Note 18 to the consolidated financial statements for further information about our leases.

Our occupancy expenses include costs associated with office space held in excess of our current requirements. This excess space, the cost of which is charged to earnings as incurred, is being held for potential growth or to replace currently occupied space that we may exit in the future. We regularly evaluate our current and future space capacity in relation to current and projected staffing levels. For the year ended December 2012, total occupancy expenses for space held in excess of our current requirements were not material. In addition, for the year ended December 2012, we incurred exit costs of $17 million related to our office space. We may incur exit costs (included in "Depreciation and amortization" and "Occupancy") in the future to the extent we (i) reduce our space capacity or (ii) commit to, or occupy, new properties in the locations in which we operate and, consequently, dispose of existing space that had been held for potential growth. These exit costs may be material to our results of operations in a given period.

Overview and Structure of Risk Management

Overview

We believe that effective risk management is of primary importance to the success of the firm. Accordingly, we have comprehensive risk management processes through which we monitor, evaluate and manage the risks we assume in conducting our activities. These include market, credit, liquidity, operational, legal, regulatory and reputational risk exposures. Our risk management framework is built around three core components: governance, processes and people.

Governance. Risk management governance starts with our Board, which plays an important role in reviewing and approving risk management policies and practices, both directly and through its Risk Committee, which consists of all of our independent directors. The Board also receives regular briefings on firmwide risks, including market risk, liquidity risk, credit risk and operational risk from our independent control and support functions, including the chief risk officer. The chief risk officer, as part of the review of the firmwide risk package, regularly advises the Risk Committee of the Board of relevant risk metrics and material exposures. Next, at the most senior levels of the firm, our leaders are experienced risk managers, with a sophisticated and detailed understanding of the risks we take. Our senior managers lead and participate in risk-oriented committees, as do the leaders of our independent control and support functions — including those in internal audit, compliance, controllers, credit risk management, human capital management, legal, market risk management, operations, operational risk management, tax, technology and treasury.

The firm's governance structure provides the protocol and responsibility for decision-making on risk management issues and ensures implementation of those decisions. We make extensive use of risk-related committees that meet regularly and serve as an important means to facilitate and foster ongoing discussions to identify, manage and mitigate risks.

We maintain strong communication about risk and we have a culture of collaboration in decision-making among the revenue-producing units, independent control and support functions, committees and senior management. While we believe that the first line of defense in managing risk rests with the managers in our revenue-producing units, we dedicate extensive resources to independent control and support functions in order to ensure a strong oversight structure and an appropriate segregation of duties. We regularly reinforce the firm's strong culture of escalation and accountability across all divisions and functions.

Processes. We maintain various processes and procedures that are critical components of our risk management. First and foremost is our daily discipline of marking substantially all of the firm's inventory to current market levels. Goldman Sachs carries its inventory at fair value, with changes in valuation reflected immediately in our risk management systems and in net revenues. We do so because we believe this discipline is one of the most effective tools for assessing and managing risk and that it provides transparent and realistic insight into our financial exposures.

We also apply a rigorous framework of limits to control risk across multiple transactions, products, businesses and markets. This includes setting credit and market risk limits at a variety of levels and monitoring these limits on a daily basis. Limits are typically set at levels that will be periodically exceeded, rather than at levels which reflect our maximum risk appetite. This fosters an ongoing dialogue on risk among revenue-producing units, independent control and support functions, committees and senior management, as well as rapid escalation of risk-related matters. See "Market Risk Management" and "Credit Risk Management" for further information on our risk limits.

Active management of our positions is another important process. Proactive mitigation of our market and credit exposures minimizes the risk that we will be required to take outsized actions during periods of stress.

We also focus on the rigor and effectiveness of the firm's risk systems. The goal of our risk management technology is to get the right information to the right people at the right time, which requires systems that are comprehensive, reliable and timely. We devote significant time and resources to our risk management technology to ensure that it consistently provides us with complete, accurate and timely information.

People. Even the best technology serves only as a tool for helping to make informed decisions in real time about the risks we are taking. Ultimately, effective risk management requires our people to interpret our risk data on an ongoing and timely basis and adjust risk positions accordingly. In both our revenue-producing units and our independent control and support functions, the experience of our professionals, and their understanding of the nuances and limitations of each risk measure, guide the firm in assessing exposures and maintaining them within prudent levels.

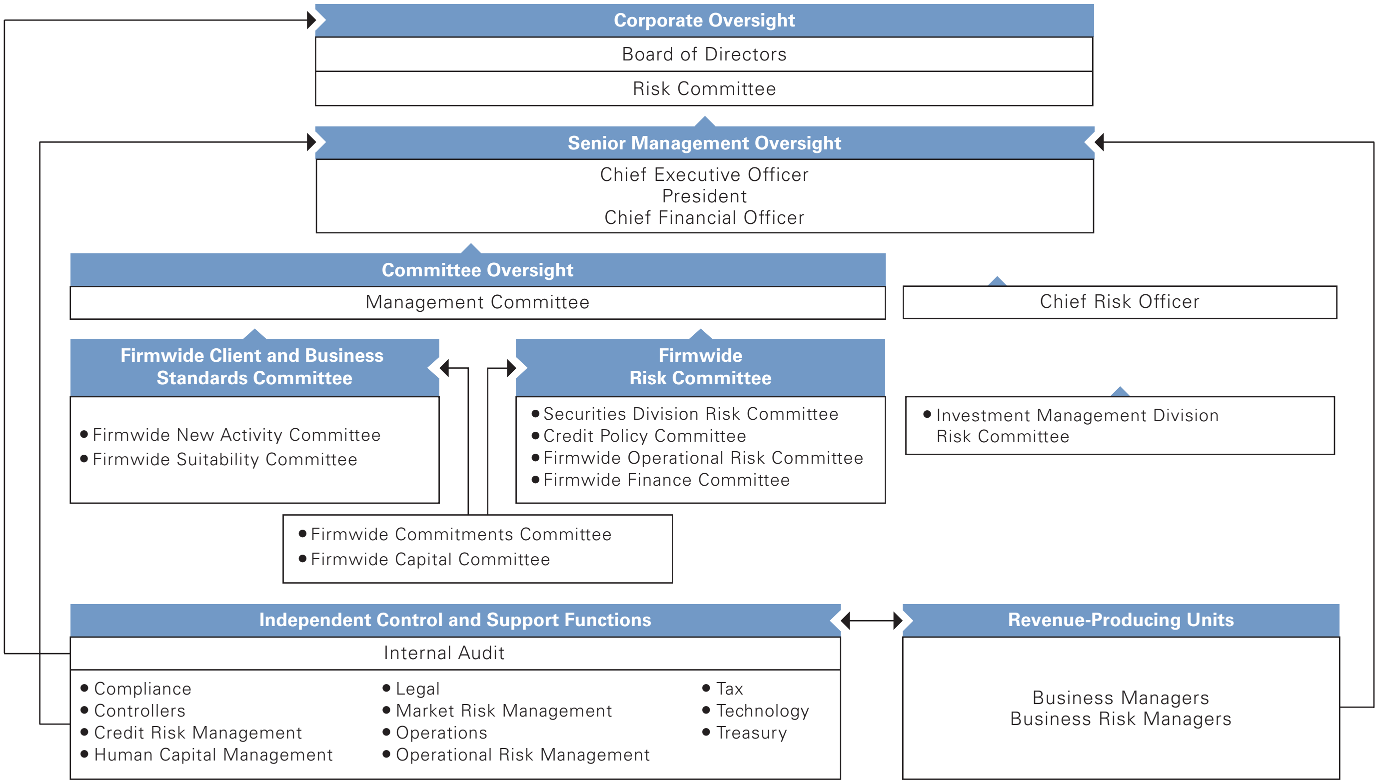
Structure

Ultimate oversight of risk is the responsibility of the firm's Board. The Board oversees risk both directly and through its Risk Committee. Within the firm, a series of committees with specific risk management mandates have oversight or decision-making responsibilities for risk management activities. Committee membership generally consists of senior managers from both our revenue-producing units and our independent control and support functions. We have established procedures for these committees to ensure that appropriate information barriers are in place. Our primary risk committees, most of which also have additional sub-committees or working groups, are described below. In addition to these committees, we have other risk-oriented committees which provide oversight for different businesses, activities, products, regions and legal entities.

Membership of the firm's risk committees is reviewed regularly and updated to reflect changes in the responsibilities of the committee members. Accordingly, the length of time that members serve on the respective committees varies as determined by the committee chairs and based on the responsibilities of the members within the firm.

In addition, independent control and support functions, which report to the chief financial officer, the general counsel and the chief administrative officer, or in the case of Internal Audit, to the Audit Committee of the Board, are responsible for day-to-day oversight or monitoring of risk, as discussed in greater detail in the following sections. Internal Audit, which includes professionals with a broad range of audit and industry experience, including risk management expertise, is responsible for independently assessing and validating key controls within the risk management framework.

The chart below presents an overview of our risk management governance structure, highlighting the oversight of our Board, our key risk-related committees and the independence of our control and support functions.



Management Committee. The Management Committee oversees the global activities of the firm, including all of the firm's independent control and support functions. It provides this oversight directly and through authority delegated to committees it has established. This committee is comprised of the most senior leaders of the firm, and is chaired by the firm's chief executive officer. The Management Committee has established various committees with delegated authority and the chairperson of the Management Committee appoints the chairpersons of these committees. Most members of the Management Committee are also members of other firmwide, divisional and regional committees. The following are the committees that are principally involved in firmwide risk management.

Firmwide Client and Business Standards Committee. The Firmwide Client and Business Standards Committee assesses and makes determinations regarding business standards and practices, reputational risk management, client relationships and client service, is chaired by the firm's president and chief operating officer, and reports to the Management Committee. This committee also has responsibility for overseeing the implementation of the recommendations of the Business Standards Committee. This committee has established the following two risk-related committees that report to it:

- **Firmwide New Activity Committee.** The Firmwide New Activity Committee is responsible for reviewing new activities and for establishing a process to identify and review previously approved activities that are significant and that have changed in complexity and/or structure or present different reputational and suitability concerns over time to consider whether these activities remain appropriate. This committee is co-chaired by the firm's head of operations/chief operating officer for Europe, Middle East and Africa and the chief administrative officer of our Investment Management Division who are appointed by the Firmwide Client and Business Standards Committee chairperson.
- **Firmwide Suitability Committee.** The Firmwide Suitability Committee is responsible for setting standards and policies for product, transaction and client suitability and providing a forum for consistency across divisions, regions and products on suitability assessments. This committee also reviews suitability matters escalated from other firm committees. This committee is co-chaired by the firm's international general counsel and the co-head of our Investment Management Division who are appointed by the Firmwide Client and Business Standards Committee chairperson.

Firmwide Risk Committee. The Firmwide Risk Committee is globally responsible for the ongoing monitoring and control of the firm's financial risks. Through both direct and delegated authority, the Firmwide Risk Committee approves firmwide, product, divisional and business-level limits for both market and credit risks, approves sovereign credit risk limits and reviews results of stress tests and scenario analyses. This committee is co-chaired by the firm's chief financial officer and a senior managing director from the firm's executive office, and reports to the Management Committee. The following four committees report to the Firmwide Risk Committee. The chairperson of the Securities Division Risk Committee is appointed by the chairpersons of the Firmwide Risk Committee; the chairpersons of the Credit Policy and Firmwide Operational Risk Committees are appointed by the firm's chief risk officer; and the chairpersons of the Firmwide Finance Committee are appointed by the Firmwide Risk Committee.

- **Securities Division Risk Committee.** The Securities Division Risk Committee sets market risk limits, subject to overall firmwide risk limits, for the Securities Division based on a number of risk measures, including but not limited to VaR, stress tests, scenario analyses and balance sheet levels. This committee is chaired by the chief risk officer of our Securities Division.
- **Credit Policy Committee.** The Credit Policy Committee establishes and reviews broad firmwide credit policies and parameters that are implemented by our Credit Risk Management department (Credit Risk Management). This committee is chaired by the firm's chief credit officer.
- **Firmwide Operational Risk Committee.** The Firmwide Operational Risk Committee provides oversight of the ongoing development and implementation of our operational risk policies, framework and methodologies, and monitors the effectiveness of operational risk management. This committee is chaired by a managing director in Credit Risk Management.
- **Firmwide Finance Committee.** The Firmwide Finance Committee has oversight of firmwide liquidity, the size and composition of our balance sheet and capital base, and our credit ratings. This committee regularly reviews and discusses our liquidity, balance sheet, funding position and capitalization in the context of current events, risks and exposures, and regulatory requirements. This committee is also responsible for reviewing and approving balance sheet limits and the size of our GCE. This committee is co-chaired by the firm's chief financial officer and the firm's global treasurer.

The following committees report jointly to the Firmwide Risk Committee and the Firmwide Client and Business Standards Committee:

- **Firmwide Commitments Committee.** The Firmwide Commitments Committee reviews the firm's underwriting and distribution activities with respect to equity and equity-related product offerings, and sets and maintains policies and procedures designed to ensure that legal, reputational, regulatory and business standards are maintained on a global basis. In addition to reviewing specific transactions, this committee periodically conducts general strategic reviews of sectors and products and establishes policies in connection with transaction practices. This committee is co-chaired by the firm's senior strategy officer and the co-head of Global Mergers & Acquisitions who are appointed by the Firmwide Client and Business Standards Committee chairperson.
- **Firmwide Capital Committee.** The Firmwide Capital Committee provides approval and oversight of debt-related transactions, including principal commitments of the firm's capital. This committee aims to ensure that business and reputational standards for underwritings and capital commitments are maintained on a global basis. This committee is co-chaired by the firm's global treasurer and the head of credit finance for Europe, Middle East and Africa who are appointed by the Firmwide Risk Committee chairpersons.

Investment Management Division Risk Committee. The Investment Management Division Risk Committee is responsible for the ongoing monitoring and control of global market, counterparty credit and liquidity risks associated with the activities of our investment management businesses. The head of Investment Management Division risk management is the chair of this committee. The Investment Management Division Risk Committee reports to the firm's chief risk officer.

Conflicts Management

Conflicts of interest and the firm's approach to dealing with them are fundamental to our client relationships, our reputation and our long-term success. The term "conflict of interest" does not have a universally accepted meaning, and conflicts can arise in many forms within a business or between businesses. The responsibility for identifying potential conflicts, as well as complying with the firm's policies and procedures, is shared by the entire firm.

We have a multilayered approach to resolving conflicts and addressing reputational risk. The firm's senior management oversees policies related to conflicts resolution. The firm's senior management, the Business Selection and Conflicts Resolution Group, the Legal Department and Compliance Division, the Firmwide Client and Business Standards Committee and other internal committees all play roles in the formulation of policies, standards and principles and assist in making judgments regarding the appropriate resolution of particular conflicts. Resolving potential conflicts necessarily depends on the facts and circumstances of a particular situation and the application of experienced and informed judgment.

At the transaction level, various people and groups have roles. As a general matter, the Business Selection and Conflicts Resolution Group reviews all financing and advisory assignments in Investment Banking and investing, lending and other activities of the firm. Various transaction oversight committees, such as the Firmwide Capital, Commitments and Suitability Committees and other committees across the firm, also review new underwritings, loans, investments and structured products. These committees work with internal and external lawyers and the Compliance Division to evaluate and address any actual or potential conflicts.

We regularly assess our policies and procedures that address conflicts of interest in an effort to conduct our business in accordance with the highest ethical standards and in compliance with all applicable laws, rules, and regulations.

Liquidity Risk Management

Liquidity is of critical importance to financial institutions. Most of the recent failures of financial institutions have occurred in large part due to insufficient liquidity. Accordingly, the firm has in place a comprehensive and conservative set of liquidity and funding policies to address both firm-specific and broader industry or market liquidity events. Our principal objective is to be able to fund the firm and to enable our core businesses to continue to serve clients and generate revenues, even under adverse circumstances.

We manage liquidity risk according to the following principles:

Excess Liquidity. We maintain substantial excess liquidity to meet a broad range of potential cash outflows and collateral needs in a stressed environment.

Asset-Liability Management. We assess anticipated holding periods for our assets and their expected liquidity in a stressed environment. We manage the maturities and diversity of our funding across markets, products and counterparties, and seek to maintain liabilities of appropriate tenor relative to our asset base.

Contingency Funding Plan. We maintain a contingency funding plan to provide a framework for analyzing and responding to a liquidity crisis situation or periods of market stress. This framework sets forth the plan of action to fund normal business activity in emergency and stress situations. These principles are discussed in more detail below.

Excess Liquidity

Our most important liquidity policy is to pre-fund our estimated potential cash and collateral needs during a liquidity crisis and hold this excess liquidity in the form of unencumbered, highly liquid securities and cash. We believe that the securities held in our global core excess would be readily convertible to cash in a matter of days, through liquidation, by entering into repurchase agreements or from maturities of reverse repurchase agreements, and that this cash would allow us to meet immediate obligations without needing to sell other assets or depend on additional funding from credit-sensitive markets.

As of December 2012 and December 2011, the fair value of the securities and certain overnight cash deposits included in our GCE totaled \$174.62 billion and \$171.58 billion, respectively. Based on the results of our internal liquidity risk model, discussed below, as well as our consideration of other factors including, but not limited to, a qualitative assessment of the condition of the financial markets and the firm, we believe our liquidity position as of December 2012 was appropriate.

The table below presents the fair value of the securities and certain overnight cash deposits that are included in our GCE.

	Average for the Year Ended December	
in millions	**2012**	2011
U.S. dollar-denominated	**$125,111**	$125,668
Non-U.S. dollar-denominated	**46,984**	40,291
Total	**$172,095**	$165,959

The U.S. dollar-denominated excess is composed of (i) unencumbered U.S. government and federal agency obligations (including highly liquid U.S. federal agency mortgage-backed obligations), all of which are eligible as collateral in Federal Reserve open market operations and (ii) certain overnight U.S. dollar cash deposits. The non-U.S. dollar-denominated excess is composed of only unencumbered German, French, Japanese and United Kingdom government obligations and certain overnight cash deposits in highly liquid currencies. We strictly limit our excess liquidity to this narrowly defined list of securities and cash because they are highly liquid, even in a difficult funding environment. We do not include other potential sources of excess liquidity, such as less liquid unencumbered securities or committed credit facilities, in our GCE.

The table below presents the fair value of our GCE by asset class.

in millions	Average for the Year Ended December 2012	2011
Overnight cash deposits	$ 52,233	$ 34,622
U.S. government obligations	72,379	88,528
U.S. federal agency obligations, including highly liquid U.S. federal agency mortgage-backed obligations	2,313	5,018
German, French, Japanese and United Kingdom government obligations	45,170	37,791
Total	$172,095	$165,959

The GCE is held at Group Inc. and our major broker-dealer and bank subsidiaries, as presented in the table below.

in millions	Average for the Year Ended December 2012	2011
Group Inc.	$ 37,405	$ 49,548
Major broker-dealer subsidiaries	78,229	75,086
Major bank subsidiaries	56,461	41,325
Total	$172,095	$165,959

Our GCE reflects the following principles:

- The first days or weeks of a liquidity crisis are the most critical to a company's survival.
- Focus must be maintained on all potential cash and collateral outflows, not just disruptions to financing flows. Our businesses are diverse, and our liquidity needs are determined by many factors, including market movements, collateral requirements and client commitments, all of which can change dramatically in a difficult funding environment.
- During a liquidity crisis, credit-sensitive funding, including unsecured debt and some types of secured financing agreements, may be unavailable, and the terms (e.g., interest rates, collateral provisions and tenor) or availability of other types of secured financing may change.
- As a result of our policy to pre-fund liquidity that we estimate may be needed in a crisis, we hold more unencumbered securities and have larger debt balances than our businesses would otherwise require. We believe that our liquidity is stronger with greater balances of highly liquid unencumbered securities, even though it increases our total assets and our funding costs.

We believe that our GCE provides us with a resilient source of funds that would be available in advance of potential cash and collateral outflows and gives us significant flexibility in managing through a difficult funding environment.

In order to determine the appropriate size of our GCE, we use an internal liquidity model, referred to as the Modeled Liquidity Outflow, which captures and quantifies the firm's liquidity risks. We also consider other factors including, but not limited to, an assessment of our potential intraday liquidity needs and a qualitative assessment of the condition of the financial markets and the firm.

We distribute our GCE across entities, asset types, and clearing agents to provide us with sufficient operating liquidity to ensure timely settlement in all major markets, even in a difficult funding environment.

We maintain our GCE to enable us to meet current and potential liquidity requirements of our parent company, Group Inc., and our major broker-dealer and bank subsidiaries. The Modeled Liquidity Outflow incorporates a consolidated requirement as well as a standalone requirement for each of our major broker-dealer and bank subsidiaries. Liquidity held directly in each of these subsidiaries is intended for use only by that subsidiary to meet its liquidity requirements and is assumed not to be available to Group Inc. unless (i) legally provided for and (ii) there are no additional regulatory, tax or other restrictions. We hold a portion of our GCE directly at Group Inc. to support consolidated requirements not accounted for in the major subsidiaries. In addition to the GCE, we maintain operating cash balances in several of our other operating entities, primarily for use in specific currencies, entities, or jurisdictions where we do not have immediate access to parent company liquidity.

In addition to our GCE, we have a significant amount of other unencumbered cash and financial instruments, including other government obligations, high-grade money market securities, corporate obligations, marginable equities, loans and cash deposits not included in our GCE. The fair value of these assets averaged $87.09 billion and $83.32 billion for the years ended December 2012 and December 2011, respectively. We do not consider these assets liquid enough to be eligible for our GCE liquidity pool and therefore conservatively do not assume we will generate liquidity from these assets in our Modeled Liquidity Outflow.

Modeled Liquidity Outflow. Our Modeled Liquidity Outflow is based on a scenario that includes both a market-wide stress and a firm-specific stress, characterized by the following qualitative elements:

- Severely challenged market environments, including low consumer and corporate confidence, financial and political instability, adverse changes in market values, including potential declines in equity markets and widening of credit spreads.
- A firm-specific crisis potentially triggered by material losses, reputational damage, litigation, executive departure, and/or a ratings downgrade.

The following are the critical modeling parameters of the Modeled Liquidity Outflow:

- Liquidity needs over a 30-day scenario.
- A two-notch downgrade of the firm's long-term senior unsecured credit ratings.
- A combination of contractual outflows, such as upcoming maturities of unsecured debt, and contingent outflows (e.g., actions though not contractually required, we may deem necessary in a crisis). We assume that most contingent outflows will occur within the initial days and weeks of a crisis.
- No issuance of equity or unsecured debt.
- No support from government funding facilities. Although we have access to various central bank funding programs, we do not assume reliance on them as a source of funding in a liquidity crisis.
- Maintenance of our normal business levels. We do not assume asset liquidation, other than the GCE.

The Modeled Liquidity Outflow is calculated and reported to senior management on a daily basis. We regularly refine our model to reflect changes in market or economic conditions and the firm's business mix.

The potential contractual and contingent cash and collateral outflows covered in our Modeled Liquidity Outflow include:

Unsecured Funding

- Contractual: All upcoming maturities of unsecured long-term debt, commercial paper, promissory notes and other unsecured funding products. We assume that we will be unable to issue new unsecured debt or rollover any maturing debt.
- Contingent: Repurchases of our outstanding long-term debt, commercial paper and hybrid financial instruments in the ordinary course of business as a market maker.

Deposits

- Contractual: All upcoming maturities of term deposits. We assume that we will be unable to raise new term deposits or rollover any maturing term deposits.
- Contingent: Withdrawals of bank deposits that have no contractual maturity. The withdrawal assumptions reflect, among other factors, the type of deposit, whether the deposit is insured or uninsured, and the firm's relationship with the depositor.

Secured Funding

- Contractual: A portion of upcoming contractual maturities of secured funding due to either the inability to refinance or the ability to refinance only at wider haircuts (i.e., on terms which require us to post additional collateral). Our assumptions reflect, among other factors, the quality of the underlying collateral, counterparty roll probabilities (our assessment of the counterparty's likelihood of continuing to provide funding on a secured basis at the maturity of the trade) and counterparty concentration.
- Contingent: A decline in value of financial assets pledged as collateral for financing transactions, which would necessitate additional collateral postings under those transactions.

OTC Derivatives

- Contingent: Collateral postings to counterparties due to adverse changes in the value of our OTC derivatives.
- Contingent: Other outflows of cash or collateral related to OTC derivatives, including the impact of trade terminations, collateral substitutions, collateral disputes, collateral calls or termination payments required by a two-notch downgrade in our credit ratings, and collateral that has not been called by counterparties, but is available to them.

Exchange-Traded Derivatives

- Contingent: Variation margin postings required due to adverse changes in the value of our outstanding exchange-traded derivatives.
- Contingent: An increase in initial margin and guaranty fund requirements by derivative clearing houses.

Customer Cash and Securities

- Contingent: Liquidity outflows associated with our prime brokerage business, including withdrawals of customer credit balances, and a reduction in customer short positions, which serve as a funding source for long positions.

Unfunded Commitments

- Contingent: Draws on our unfunded commitments. Draw assumptions reflect, among other things, the type of commitment and counterparty.

Other

- Other upcoming large cash outflows, such as tax payments.

Asset-Liability Management

Our liquidity risk management policies are designed to ensure we have a sufficient amount of financing, even when funding markets experience persistent stress. We seek to maintain a long-dated and diversified funding profile, taking into consideration the characteristics and liquidity profile of our assets.

Our approach to asset-liability management includes:

- Conservatively managing the overall characteristics of our funding book, with a focus on maintaining long-term, diversified sources of funding in excess of our current requirements. See "Balance Sheet and Funding Sources — Funding Sources" for additional details.
- Actively managing and monitoring our asset base, with particular focus on the liquidity, holding period and our ability to fund assets on a secured basis. This enables us to determine the most appropriate funding products and tenors. See "Balance Sheet and Funding Sources — Balance Sheet Management" for more detail on our balance sheet management process and "— Funding Sources — Secured Funding" for more detail on asset classes that may be harder to fund on a secured basis.
- Raising secured and unsecured financing that has a long tenor relative to the liquidity profile of our assets. This reduces the risk that our liabilities will come due in advance of our ability to generate liquidity from the sale of our assets. Because we maintain a highly liquid balance sheet, the holding period of certain of our assets may be materially shorter than their contractual maturity dates.

Our goal is to ensure that the firm maintains sufficient liquidity to fund its assets and meet its contractual and contingent obligations in normal times as well as during periods of market stress. Through our dynamic balance sheet management process (see "Balance Sheet and Funding Sources — Balance Sheet Management"), we use actual and projected asset balances to determine secured and unsecured funding requirements. Funding plans are reviewed and approved by the Firmwide Finance Committee on a quarterly basis. In addition, senior managers in our independent control and support functions regularly analyze, and the Firmwide Finance Committee reviews, our consolidated total capital position (unsecured long-term borrowings plus total shareholders' equity) so that we maintain a level of long-term funding that is sufficient to meet our long-term financing requirements. In a liquidity crisis, we would first use our GCE in order to avoid reliance on asset sales (other than our GCE). However, we recognize that orderly asset sales may be prudent or necessary in a severe or persistent liquidity crisis.

Subsidiary Funding Policies. The majority of our unsecured funding is raised by Group Inc. which lends the necessary funds to its subsidiaries, some of which are regulated, to meet their asset financing, liquidity and capital requirements. In addition, Group Inc. provides its regulated subsidiaries with the necessary capital to meet their regulatory requirements. The benefits of this approach to subsidiary funding are enhanced control and greater flexibility to meet the funding requirements of our subsidiaries. Funding is also raised at the subsidiary level through a variety of products, including secured funding, unsecured borrowings and deposits.

Our intercompany funding policies assume that, unless legally provided for, a subsidiary's funds or securities are not freely available to its parent company or other subsidiaries. In particular, many of our subsidiaries are subject to laws that authorize regulatory bodies to block or reduce the flow of funds from those subsidiaries to Group Inc. Regulatory action of that kind could impede access to funds that Group Inc. needs to make payments on its obligations. Accordingly, we assume that the capital provided to our regulated subsidiaries is not available to Group Inc. or other subsidiaries and any other financing provided to our regulated subsidiaries is not available until the maturity of such financing.

Group Inc. has provided substantial amounts of equity and subordinated indebtedness, directly or indirectly, to its regulated subsidiaries. For example, as of December 2012, Group Inc. had $29.52 billion of equity and subordinated indebtedness invested in GS&Co., its principal U.S. registered broker-dealer; $29.45 billion invested in GSI, a regulated U.K. broker-dealer; $2.62 billion invested in GSEC, a U.S. registered broker-dealer; $3.78 billion invested in Goldman Sachs Japan Co., Ltd., a regulated Japanese broker-dealer; and $20.67 billion invested in GS Bank USA, a regulated New York State-chartered bank. Group Inc. also provided, directly or indirectly, $68.44 billion of unsubordinated loans and $11.37 billion of collateral to these entities, substantially all of which was to GS&Co., GSI and GS Bank USA, as of December 2012. In addition, as of December 2012, Group Inc. had significant amounts of capital invested in and loans to its other regulated subsidiaries.

Contingency Funding Plan

The Goldman Sachs contingency funding plan sets out the plan of action we would use to fund business activity in crisis situations and periods of market stress. The contingency funding plan outlines a list of potential risk factors, key reports and metrics that are reviewed on an ongoing basis to assist in assessing the severity of, and managing through, a liquidity crisis and/or market dislocation. The contingency funding plan also describes in detail the firm's potential responses if our assessments indicate that the firm has entered a liquidity crisis, which include pre-funding for what we estimate will be our potential cash and collateral needs as well as utilizing secondary sources of liquidity. Mitigants and action items to address specific risks which may arise are also described and assigned to individuals responsible for execution.

The contingency funding plan identifies key groups of individuals to foster effective coordination, control and distribution of information, all of which are critical in the management of a crisis or period of market stress. The contingency funding plan also details the responsibilities of these groups and individuals, which include making and disseminating key decisions, coordinating all contingency activities throughout the duration of the crisis or period of market stress, implementing liquidity maintenance activities and managing internal and external communication.

Proposed Liquidity Framework

The Basel Committee on Banking Supervision's international framework for liquidity risk measurement, standards and monitoring calls for imposition of a liquidity coverage ratio, designed to ensure that the banking entity maintains an adequate level of unencumbered high-quality liquid assets based on expected cash outflows under an acute liquidity stress scenario, and a net stable funding ratio, designed to promote more medium- and long-term funding of the assets and activities of banking entities over a one-year time horizon. While the principles behind the new framework are broadly consistent with our current liquidity management framework, it is possible that the implementation of these standards could impact our liquidity and funding requirements and practices. Under the Basel Committee framework, the liquidity coverage ratio would be introduced on January 1, 2015; however there would be a phase-in period whereby firms would have a 60% minimum in 2015 which would be raised 10% per year until it reaches 100% in 2019. The net stable funding ratio is not expected to be introduced as a requirement until January 1, 2018.

Credit Ratings

The table below presents the unsecured credit ratings and outlook of Group Inc.

	As of December 2012					
	Short-Term Debt	Long-Term Debt	Subordinated Debt	Trust Preferred [1]	Preferred Stock	Ratings Outlook
DBRS, Inc.	R-1 (middle)	A (high)	A	A	BBB [3]	Stable
Fitch, Inc.	F1	A [2]	A-	BBB-	BB+ [3]	Stable
Moody's Investors Service (Moody's)	P-2	A3 [2]	Baa1	Baa3	Ba2 [3]	Negative [4]
Standard & Poor's Ratings Services (S&P)	A-2	A- [2]	BBB+	BB+	BB+ [3]	Negative
Rating and Investment Information, Inc.	a-1	A+	A	N/A	N/A	Negative

1. Trust preferred securities issued by Goldman Sachs Capital I.

2. Includes the senior guaranteed trust securities issued by Murray Street Investment Trust I and Vesey Street Investment Trust I.

3. Includes Group Inc.'s non-cumulative preferred stock and the APEX issued by Goldman Sachs Capital II and Goldman Sachs Capital III.

4. The ratings outlook for trust preferred and preferred stock is stable.

The table below presents the unsecured credit ratings of GS Bank USA, GS&Co. and GSI.

	As of December 2012			
	Short-Term Debt	Long-Term Debt	Short-Term Bank Deposits	Long-Term Bank Deposits
Fitch, Inc.				
GS Bank USA	F1	A	F1	A+
GS&Co.	F1	A	N/A	N/A
Moody's				
GS Bank USA	P-1	A2	P-1	A2
S&P				
GS Bank USA	A-1	A	N/A	N/A
GS&Co.	A-1	A	N/A	N/A
GSI	A-1	A	N/A	N/A

On January 24, 2013, Fitch, Inc. assigned GSI a rating of F1 for short-term debt and A for long-term debt.

We rely on the short-term and long-term debt capital markets to fund a significant portion of our day-to-day operations and the cost and availability of debt financing is influenced by our credit ratings. Credit ratings are also important when we are competing in certain markets, such as OTC derivatives, and when we seek to engage in longer-term transactions. See "Certain Risk Factors That May Affect Our Businesses" below and "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K for a discussion of the risks associated with a reduction in our credit ratings.

We believe our credit ratings are primarily based on the credit rating agencies' assessment of:

- our liquidity, market, credit and operational risk management practices;
- the level and variability of our earnings;
- our capital base;
- our franchise, reputation and management;
- our corporate governance; and
- the external operating environment, including the assumed level of government support.

Certain of the firm's derivatives have been transacted under bilateral agreements with counterparties who may require us to post collateral or terminate the transactions based on changes in our credit ratings. We assess the impact of these bilateral agreements by determining the collateral or termination payments that would occur assuming a downgrade by all rating agencies. A downgrade by any one rating agency, depending on the agency's relative ratings of the firm at the time of the downgrade, may have an impact which is comparable to the impact of a downgrade by all rating agencies. We allocate a portion of our GCE to ensure we would be able to make the additional collateral or termination payments that may be required in the event of a two-notch reduction in our long-term credit ratings, as well as collateral that has not been called by counterparties, but is available to them. The table below presents the additional collateral or termination payments that could have been called at the reporting date by counterparties in the event of a one-notch and two-notch downgrade in our credit ratings.

	As of December	
in millions	**2012**	2011
Additional collateral or termination payments for a one-notch downgrade	**$1,534**	$1,303
Additional collateral or termination payments for a two-notch downgrade	**2,500**	2,183

Cash Flows

As a global financial institution, our cash flows are complex and bear little relation to our net earnings and net assets. Consequently, we believe that traditional cash flow analysis is less meaningful in evaluating our liquidity position than the excess liquidity and asset-liability management policies described above. Cash flow analysis may, however, be helpful in highlighting certain macro trends and strategic initiatives in our businesses.

Year Ended December 2012. Our cash and cash equivalents increased by $16.66 billion to $72.67 billion at the end of 2012. We generated $9.14 billion in net cash from operating and investing activities. We generated $7.52 billion in net cash from financing activities from an increase in bank deposits, partially offset by net repayments of unsecured and secured long-term borrowings.

Year Ended December 2011. Our cash and cash equivalents increased by $16.22 billion to $56.01 billion at the end of 2011. We generated $23.13 billion in net cash from operating and investing activities. We used net cash of $6.91 billion for financing activities, primarily for repurchases of our Series G Preferred Stock and common stock, partially offset by an increase in bank deposits.

Year Ended December 2010. Our cash and cash equivalents increased by $1.50 billion to $39.79 billion at the end of 2010. We generated $7.84 billion in net cash from financing activities primarily from net proceeds from issuances of short-term secured financings. We used net cash of $6.34 billion for operating and investing activities, primarily to fund an increase in securities purchased under agreements to resell and an increase in cash and securities segregated for regulatory and other purposes, partially offset by cash generated from a decrease in securities borrowed.

Market Risk Management

Overview

Market risk is the risk of loss in the value of our inventory due to changes in market prices. We hold inventory primarily for market making for our clients and for our investing and lending activities. Our inventory therefore changes based on client demands and our investment opportunities. Our inventory is accounted for at fair value and therefore fluctuates on a daily basis, with the related gains and losses included in "Market making," and "Other principal transactions." Categories of market risk include the following:

- Interest rate risk: results from exposures to changes in the level, slope and curvature of yield curves, the volatilities of interest rates, mortgage prepayment speeds and credit spreads.
- Equity price risk: results from exposures to changes in prices and volatilities of individual equities, baskets of equities and equity indices.
- Currency rate risk: results from exposures to changes in spot prices, forward prices and volatilities of currency rates.
- Commodity price risk: results from exposures to changes in spot prices, forward prices and volatilities of commodities, such as electricity, natural gas, crude oil, petroleum products, and precious and base metals.

Market Risk Management Process

We manage our market risk by diversifying exposures, controlling position sizes and establishing economic hedges in related securities or derivatives. This includes:

- accurate and timely exposure information incorporating multiple risk metrics;
- a dynamic limit setting framework; and
- constant communication among revenue-producing units, risk managers and senior management.

Market Risk Management, which is independent of the revenue-producing units and reports to the firm's chief risk officer, has primary responsibility for assessing, monitoring and managing market risk at the firm. We monitor and control risks through strong firmwide oversight and independent control and support functions across the firm's global businesses.

Managers in revenue-producing units are accountable for managing risk within prescribed limits. These managers have in-depth knowledge of their positions, markets and the instruments available to hedge their exposures.

Managers in revenue-producing units and Market Risk Management discuss market information, positions and estimated risk and loss scenarios on an ongoing basis.

Risk Measures

Market Risk Management produces risk measures and monitors them against market risk limits set by our firm's risk committees. These measures reflect an extensive range of scenarios and the results are aggregated at trading desk, business and firmwide levels.

We use a variety of risk measures to estimate the size of potential losses for both moderate and more extreme market moves over both short-term and long-term time horizons. Risk measures used for shorter-term periods include VaR and sensitivity metrics. For longer-term horizons, our primary risk measures are stress tests. Our risk reports detail key risks, drivers and changes for each desk and business, and are distributed daily to senior management of both our revenue-producing units and our independent control and support functions.

Systems

We have made a significant investment in technology to monitor market risk including:

- an independent calculation of VaR and stress measures;
- risk measures calculated at individual position levels;
- attribution of risk measures to individual risk factors of each position;
- the ability to report many different views of the risk measures (e.g., by desk, business, product type or legal entity); and
- the ability to produce ad hoc analyses in a timely manner.

Value-at-Risk

VaR is the potential loss in value of inventory positions due to adverse market movements over a defined time horizon with a specified confidence level. We typically employ a one-day time horizon with a 95% confidence level. We use a single VaR model which captures risks including interest rates, equity prices, currency rates and commodity prices. As such, VaR facilitates comparison across portfolios of different risk characteristics. VaR also captures the diversification of aggregated risk at the firmwide level.

We are aware of the inherent limitations to VaR and therefore use a variety of risk measures in our market risk management process. Inherent limitations to VaR include:

- VaR does not estimate potential losses over longer time horizons where moves may be extreme.
- VaR does not take account of the relative liquidity of different risk positions.
- Previous moves in market risk factors may not produce accurate predictions of all future market moves.

When calculating VaR, we use historical simulations with full valuation of approximately 70,000 market factors. VaR is calculated at a position level based on simultaneously shocking the relevant market risk factors for that position. We sample from 5 years of historical data to generate the scenarios for our VaR calculation. The historical data is weighted so that the relative importance of the data reduces over time. This gives greater importance to more recent observations and reflects current asset volatilities, which improves the accuracy of our estimates of potential loss. As a result, even if our inventory positions were unchanged, our VaR would increase with increasing market volatility and vice versa.

Given its reliance on historical data, VaR is most effective in estimating risk exposures in markets in which there are no sudden fundamental changes or shifts in market conditions.

Our VaR measure does not include:

- positions that are best measured and monitored using sensitivity measures; and
- the impact of changes in counterparty and our own credit spreads on derivatives, as well as changes in our own credit spreads on unsecured borrowings for which the fair value option was elected.

Model Review and Validation

Our VaR model is subject to review and validation by our independent model validation group at least annually. This review includes:

- a critical evaluation of the model, its theoretical soundness and adequacy for intended use;
- verification of the testing strategy utilized by the model developers to ensure that the model functions as intended; and
- verification of the suitability of the calculation techniques incorporated in the model.

Our VaR model is regularly reviewed and enhanced in order to incorporate changes in the composition of inventory positions, as well as variations in market conditions. Prior to implementing significant changes to our assumptions and/or model, we perform model validation and test runs. Significant changes to our VaR model are reviewed with the firm's chief risk officer and chief financial officer, and approved by the Firmwide Risk Committee.

We evaluate the accuracy of our VaR model through daily backtesting (i.e., comparing daily trading net revenues to the VaR measure calculated as of the prior business day) at the firmwide level and for each of our businesses and major regulated subsidiaries.

Stress Testing

We use stress testing to examine risks of specific portfolios as well as the potential impact of significant risk exposures across the firm. We use a variety of stress testing techniques to calculate the potential loss from a wide range of market moves on the firm's portfolios, including sensitivity analysis, scenario analysis and firmwide stress tests. The results of our various stress tests are analyzed together for risk management purposes.

Sensitivity analysis is used to quantify the impact of a market move in a single risk factor across all positions (e.g., equity prices or credit spreads) using a variety of defined market shocks, ranging from those that could be expected over a one-day time horizon up to those that could take many months to occur. We also use sensitivity analysis to quantify the impact of the default of a single corporate entity, which captures the risk of large or concentrated exposures.

Scenario analysis is used to quantify the impact of a specified event, including how the event impacts multiple risk factors simultaneously. For example, for sovereign stress testing we calculate potential direct exposure associated with our sovereign inventory as well as the corresponding debt, equity and currency exposures associated with our non-sovereign inventory that may be impacted by the sovereign distress. When conducting scenario analysis, we typically consider a number of possible outcomes for each scenario, ranging from moderate to severely adverse market impacts. In addition, these stress tests are constructed using both historical events and forward-looking hypothetical scenarios.

Firmwide stress testing combines market, credit, operational and liquidity risks into a single combined scenario. Firmwide stress tests are primarily used to assess capital adequacy as part of the ICAAP process; however, we also ensure that firmwide stress testing is integrated into our risk governance framework. This includes selecting appropriate scenarios to use for the ICAAP process. See "Equity Capital — Internal Capital Adequacy Assessment Process" above for further information about our ICAAP process.

Unlike VaR measures, which have an implied probability because they are calculated at a specified confidence level, there is generally no implied probability that our stress test scenarios will occur. Instead, stress tests are used to model both moderate and more extreme moves in underlying market factors. When estimating potential loss, we generally assume that our positions cannot be reduced or hedged (although experience demonstrates that we are generally able to do so).

Stress test scenarios are conducted on a regular basis as part of the firm's routine risk management process and on an ad hoc basis in response to market events or concerns. Stress testing is an important part of the firm's risk management process because it allows us to quantify our exposure to tail risks, highlight potential loss concentrations, undertake risk/reward analysis, and assess and mitigate our risk positions.

Limits

We use risk limits at various levels in the firm (including firmwide, product and business) to govern risk appetite by controlling the size of our exposures to market risk. Limits are set based on VaR and on a range of stress tests relevant to the firm's exposures. Limits are reviewed frequently and amended on a permanent or temporary basis to reflect changing market conditions, business conditions or tolerance for risk.

The Firmwide Risk Committee sets market risk limits at firmwide and product levels and our Securities Division Risk Committee sets sub-limits for market-making and investing activities at a business level. The purpose of the firmwide limits is to assist senior management in controlling the firm's overall risk profile. Sub-limits set the desired maximum amount of exposure that may be managed by any particular business on a day-to-day basis without additional levels of senior management approval, effectively leaving day-to-day trading decisions to individual desk managers and traders. Accordingly, sub-limits are a management tool designed to ensure appropriate escalation rather than to establish maximum risk tolerance. Sub-limits also distribute risk among various businesses in a manner that is consistent with their level of activity and client demand, taking into account the relative performance of each area.

Our market risk limits are monitored daily by Market Risk Management, which is responsible for identifying and escalating, on a timely basis, instances where limits have been exceeded. The business-level limits that are set by the Securities Division Risk Committee are subject to the same scrutiny and limit escalation policy as the firmwide limits.

When a risk limit has been exceeded (e.g., due to changes in market conditions, such as increased volatilities or changes in correlations), it is reported to the appropriate risk committee and a discussion takes place with the relevant desk managers, after which either the risk position is reduced or the risk limit is temporarily or permanently increased.

Metrics

We analyze VaR at the firmwide level and a variety of more detailed levels, including by risk category, business, and region. The tables below present, by risk category, average daily VaR and period-end VaR, as well as the high and low VaR for the period. Diversification effect in the tables below represents the difference between total VaR and the sum of the VaRs for the four risk categories. This effect arises because the four market risk categories are not perfectly correlated.

Average Daily VaR

in millions	Year Ended December		
Risk Categories	**2012**	2011	2010
Interest rates	**$ 78**	$ 94	$ 93
Equity prices	**26**	33	68
Currency rates	**14**	20	32
Commodity prices	**22**	32	33
Diversification effect	**(54)**	(66)	(92)
Total	**$ 86**	$113	$134

Our average daily VaR decreased to $86 million in 2012 from $113 million in 2011, reflecting a decrease in the interest rates category due to lower levels of volatility, decreases in the commodity prices and currency rates categories due to reduced exposures and lower levels of volatility, and a decrease in the equity prices category due to reduced exposures. These decreases were partially offset by a decrease in the diversification benefit across risk categories.

Our average daily VaR decreased to $113 million in 2011 from $134 million in 2010, primarily reflecting decreases in the equity prices and currency rates categories, principally due to reduced exposures. These decreases were partially offset by a decrease in the diversification benefit across risk categories.

Year-End VaR and High and Low VaR

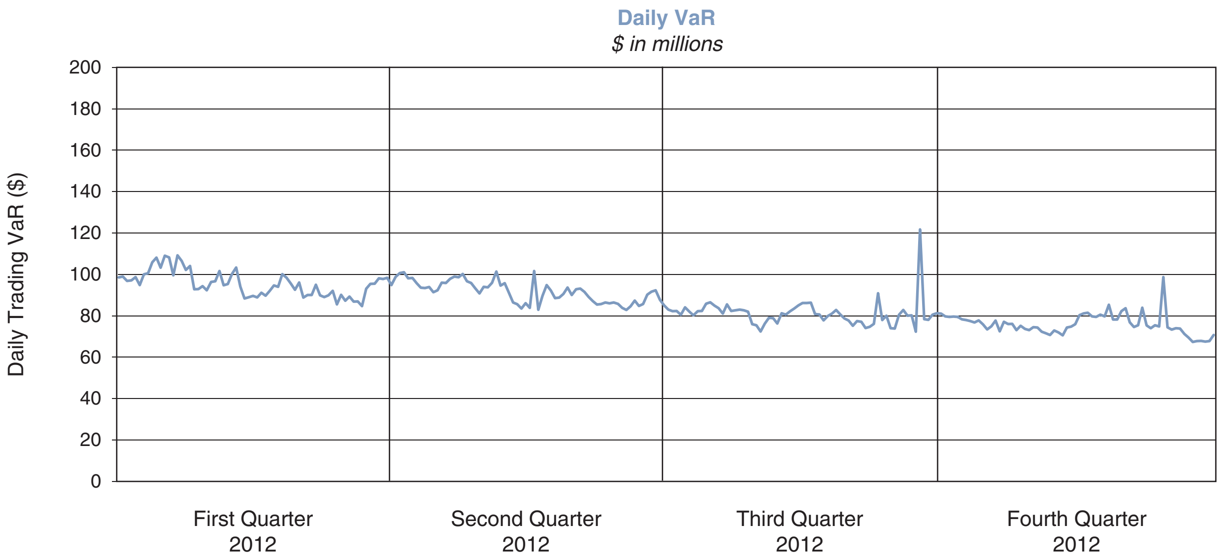
in millions	As of December		**Year Ended December 2012**	
Risk Categories	**2012**	2011	**High**	**Low**
Interest rates	**$ 64**	$100	**$103**	**$61**
Equity prices	**22**	31	**92**	**14**
Currency rates	**9**	14	**22**	**9**
Commodity prices	**18**	23	**32**	**15**
Diversification effect	**(42)**	(69)		
Total	**$ 71**	$ 99	**$122**	**$67**

Our daily VaR decreased to $71 million as of December 2012 from $99 million as of December 2011, primarily reflecting decreases in the interest rates and equity prices categories due to lower levels of volatility. These decreases were partially offset by a decrease in the diversification benefit across risk categories.

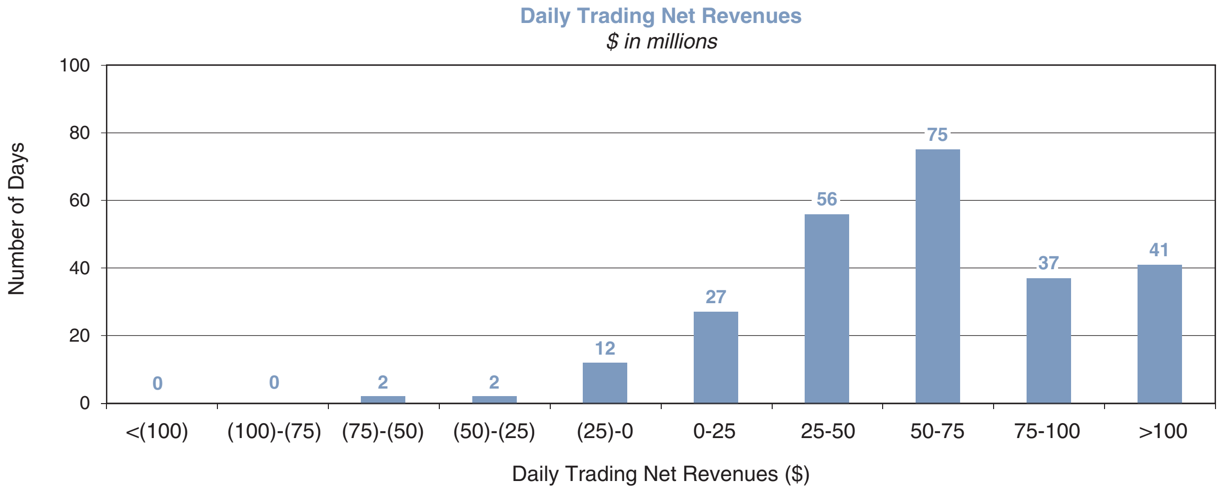
During the year ended December 2012, the firmwide VaR risk limit was not exceeded and was reduced on one occasion due to lower levels of volatility.

During the year ended December 2011, the firmwide VaR risk limit was exceeded on one occasion. It was resolved by a temporary increase in the firmwide VaR risk limit, which was subsequently made permanent due to higher levels of volatility. The firmwide VaR risk limit had previously been reduced on one occasion in 2011, reflecting lower risk utilization and the market environment.

The chart below reflects the VaR over the last four quarters.



The chart below presents the frequency distribution of our daily trading net revenues for substantially all inventory positions included in VaR for the year ended December 2012.



Daily trading net revenues are compared with VaR calculated as of the end of the prior business day. Trading losses incurred on a single day did not exceed our 95% one-day VaR during 2012. Trading losses incurred on a single day exceeded our 95% one-day VaR (i.e., a VaR exception) on three occasions during 2011.

During periods in which the firm has significantly more positive net revenue days than net revenue loss days, we expect to have fewer VaR exceptions because, under normal conditions, our business model generally produces positive net revenues. In periods in which our franchise revenues are adversely affected, we generally have more loss days, resulting in more VaR exceptions. In addition, VaR backtesting is performed against total daily market-making revenues, including bid/offer net revenues, which are more likely than not to be positive by their nature.

Sensitivity Measures

Certain portfolios and individual positions are not included in VaR because VaR is not the most appropriate risk measure. The market risk of these positions is determined by estimating the potential reduction in net revenues of a 10% decline in the underlying asset value.

The table below presents market risk for positions that are not included in VaR. These measures do not reflect diversification benefits across asset categories and therefore have not been aggregated.

Asset Categories	**10% Sensitivity**	
	Amount as of December	
in millions	**2012**	2011
ICBC	**$ 208**	$ 212
Equity (excluding ICBC) [1]	**2,263**	2,458
Debt [2]	**1,676**	1,521

1. Relates to private and restricted public equity securities, including interests in firm-sponsored funds that invest in corporate equities and real estate and interests in firm-sponsored hedge funds.
2. Primarily relates to interests in our firm-sponsored funds that invest in corporate mezzanine and senior debt instruments. Also includes loans backed by commercial and residential real estate, corporate bank loans and other corporate debt, including acquired portfolios of distressed loans.

VaR excludes the impact of changes in counterparty and our own credit spreads on derivatives as well as changes in our own credit spreads on unsecured borrowings for which the fair value option was elected. The estimated sensitivity to a one basis point increase in credit spreads (counterparty and our own) on derivatives was a $3 million gain (including hedges) as of December 2012. In addition, the estimated sensitivity to a one basis point increase in our own credit spreads on unsecured borrowings for which the fair value option was elected was a $7 million gain (including hedges) as of December 2012. However, the actual net impact of a change in our own credit spreads is also affected by the liquidity, duration and convexity (as the sensitivity is not linear to changes in yields) of those unsecured borrowings for which the fair value option was elected, as well as the relative performance of any hedges undertaken.

The firm engages in insurance activities where we reinsure and purchase portfolios of insurance risk and pension liabilities. The risks associated with these activities include, but are not limited to: equity price, interest rate, reinvestment and mortality risk. The firm mitigates risks associated with insurance activities through the use of reinsurance and hedging. Certain of the assets associated with the firm's insurance activities are included in VaR. In addition to the positions included in VaR, we held $9.07 billion of securities accounted for as available-for-sale as of December 2012, which support the firm's reinsurance business. As of December 2012, our available-for-sale securities primarily consisted of $3.63 billion of corporate debt securities with an average yield of 4%, the majority of which will mature after five years, $3.38 billion of mortgage and other asset-backed loans and securities with an average yield of 6%, the majority of which will mature after ten years, and $856 million of U.S. government and federal agency obligations with an average yield of 3%, the majority of which will mature after five years. As of December 2012, such assets were classified as held for sale and were included in "Other assets." See Note 12 to the consolidated financial statements for further information about assets held for sale. As of December 2011, we held $4.86 billion of securities accounted for as available-for-sale, primarily consisting of $1.81 billion of corporate debt securities with an average yield of 5%, the majority of which will mature after five years, $1.42 billion of mortgage and other asset-backed loans and securities with an average yield of 10%, the majority of which will mature after ten years, and $662 million of U.S. government and federal agency obligations with an average yield of 3%, the majority of which will mature after ten years.

In addition, as of December 2012 and December 2011, we had commitments and held loans for which we have obtained credit loss protection from Sumitomo Mitsui Financial Group, Inc. See Note 18 to the consolidated financial statements for further information about such lending commitments. As of December 2012, the firm also had $6.50 billion of loans held for investment which were accounted for at amortized cost and included in "Receivables from customers and counterparties," substantially all of which had floating interest rates. The estimated sensitivity to a 100 basis point increase in interest rates on such loans was $62 million of additional interest income over a 12-month period, which does not take into account the potential impact of an increase in costs to fund such loans. See Note 8 to the consolidated financial statements for further information about loans held for investment.

Additionally, we make investments accounted for under the equity method and we also make direct investments in real estate, both of which are included in "Other assets" in the consolidated statements of financial condition. Direct investments in real estate are accounted for at cost less accumulated depreciation. See Note 12 to the consolidated financial statements for information on "Other assets."

Credit Risk Management

Overview

Credit risk represents the potential for loss due to the default or deterioration in credit quality of a counterparty (e.g., an OTC derivatives counterparty or a borrower) or an issuer of securities or other instruments we hold. Our exposure to credit risk comes mostly from client transactions in OTC derivatives and loans and lending commitments. Credit risk also comes from cash placed with banks, securities financing transactions (i.e., resale and repurchase agreements and securities borrowing and lending activities) and receivables from brokers, dealers, clearing organizations, customers and counterparties.

Credit Risk Management, which is independent of the revenue-producing units and reports to the firm's chief risk officer, has primary responsibility for assessing, monitoring and managing credit risk at the firm. The Credit Policy Committee and the Firmwide Risk Committee establish and review credit policies and parameters. In addition, we hold other positions that give rise to credit risk (e.g., bonds held in our inventory and secondary bank loans). These credit risks are captured as a component of market risk measures, which are monitored and managed by Market Risk Management, consistent with other inventory positions.

Policies authorized by the Firmwide Risk Committee and the Credit Policy Committee prescribe the level of formal approval required for the firm to assume credit exposure to a counterparty across all product areas, taking into account any applicable netting provisions, collateral or other credit risk mitigants.

Credit Risk Management Process

Effective management of credit risk requires accurate and timely information, a high level of communication and knowledge of customers, countries, industries and products. Our process for managing credit risk includes:

- approving transactions and setting and communicating credit exposure limits;
- monitoring compliance with established credit exposure limits;
- assessing the likelihood that a counterparty will default on its payment obligations;
- measuring the firm's current and potential credit exposure and losses resulting from counterparty default;
- reporting of credit exposures to senior management, the Board and regulators;
- use of credit risk mitigants, including collateral and hedging; and
- communication and collaboration with other independent control and support functions such as operations, legal and compliance.

As part of the risk assessment process, Credit Risk Management performs credit reviews which include initial and ongoing analyses of our counterparties. A credit review is an independent judgment about the capacity and willingness of a counterparty to meet its financial obligations. For substantially all of our credit exposures, the core of our process is an annual counterparty review. A counterparty review is a written analysis of a counterparty's business profile and financial strength resulting in an internal credit rating which represents the probability of default on financial obligations to the firm. The determination of internal credit ratings incorporates assumptions with respect to the counterparty's future business performance, the nature and outlook for the counterparty's industry, and the economic environment. Senior personnel within Credit Risk Management, with expertise in specific industries, inspect and approve credit reviews and internal credit ratings.

Our global credit risk management systems capture credit exposure to individual counterparties and on an aggregate basis to counterparties and their subsidiaries (economic groups). These systems also provide management with comprehensive information on our aggregate credit risk by product, internal credit rating, industry, country and region.

Risk Measures and Limits

We measure our credit risk based on the potential loss in an event of non-payment by a counterparty. For derivatives and securities financing transactions, the primary measure is potential exposure, which is our estimate of the future exposure that could arise over the life of a transaction based on market movements within a specified confidence level. Potential exposure takes into account netting and collateral arrangements. For loans and lending commitments, the primary measure is a function of the notional amount of the position. We also monitor credit risk in terms of current exposure, which is the amount presently owed to the firm after taking into account applicable netting and collateral.

We use credit limits at various levels (counterparty, economic group, industry, country) to control the size of our credit exposures. Limits for counterparties and economic groups are reviewed regularly and revised to reflect changing appetites for a given counterparty or group of counterparties. Limits for industries and countries are based on the firm's risk tolerance and are designed to allow for regular monitoring, review, escalation and management of credit risk concentrations.

Stress Tests/Scenario Analysis

We use regular stress tests to calculate the credit exposures, including potential concentrations that would result from applying shocks to counterparty credit ratings or credit risk factors (e.g., currency rates, interest rates, equity prices). These shocks include a wide range of moderate and more extreme market movements. Some of our stress tests include shocks to multiple risk factors, consistent with the occurrence of a severe market or economic event. In the case of sovereign default, we estimate the direct impact of the default on our sovereign credit exposures, changes to our credit exposures arising from potential market moves in response to the default, and the impact of credit market deterioration on corporate borrowers and counterparties that may result from the sovereign default. Unlike potential exposure, which is calculated within a specified confidence level, with a stress test there is generally no assumed probability of these events occurring.

We run stress tests on a regular basis as part of our routine risk management processes and conduct tailored stress tests on an ad hoc basis in response to market developments. Stress tests are regularly conducted jointly with the firm's market and liquidity risk functions.

Risk Mitigants

To reduce our credit exposures on derivatives and securities financing transactions, we may enter into netting agreements with counterparties that permit us to offset receivables and payables with such counterparties. We may also reduce credit risk with counterparties by entering into agreements that enable us to obtain collateral from them on an upfront or contingent basis and/or to terminate transactions if the counterparty's credit rating falls below a specified level.

For loans and lending commitments, depending on the credit quality of the borrower and other characteristics of the transaction, we employ a variety of potential risk mitigants. Risk mitigants include: collateral provisions, guarantees, covenants, structural seniority of the bank loan claims and, for certain lending commitments, provisions in the legal documentation that allow the firm to adjust loan amounts, pricing, structure and other terms as market conditions change. The type and structure of risk mitigants employed can significantly influence the degree of credit risk involved in a loan.

When we do not have sufficient visibility into a counterparty's financial strength or when we believe a counterparty requires support from its parent company, we may obtain third-party guarantees of the counterparty's obligations. We may also mitigate our credit risk using credit derivatives or participation agreements.

Credit Exposures

The firm's credit exposures are described further below.

Cash and Cash Equivalents. Cash and cash equivalents include both interest-bearing and non-interest-bearing deposits. To mitigate the risk of credit loss, we place substantially all of our deposits with highly rated banks and central banks.

OTC Derivatives. Derivatives are reported on a net-by-counterparty basis (i.e., the net payable or receivable for derivative assets and liabilities for a given counterparty) when a legal right of setoff exists under an enforceable netting agreement.

Derivatives are accounted for at fair value, net of cash collateral received or posted under credit support agreements. As credit risk is an essential component of fair value, the firm includes a credit valuation adjustment (CVA) in the fair value of derivatives to reflect counterparty credit risk, as described in Note 7 to the consolidated financial statements. CVA is a function of the present value of expected exposure, the probability of counterparty default and the assumed recovery upon default.

The tables below present the distribution of our exposure to OTC derivatives by tenor, based on expected duration for mortgage-related credit derivatives and generally on remaining contractual maturity for other derivatives, both before and after the effect of collateral and netting agreements. Receivable and payable balances for the same counterparty across tenor categories are netted under enforceable netting agreements, and cash collateral received is netted under credit support agreements. Receivable and payable balances with the same counterparty in the same tenor category are netted within such tenor category. The categories shown reflect our internally determined public rating agency equivalents.

in millions	As of December 2012						
Credit Rating Equivalent	**0 - 12 Months**	**1 - 5 Years**	**5 Years or Greater**	**Total**	**Netting**	**Exposure**	**Exposure Net of Collateral**
AAA/Aaa	**$ 494**	**$ 1,934**	**$ 2,778**	**$ 5,206**	**$ (1,476)**	**$ 3,730**	**$ 3,443**
AA/Aa2	**4,631**	**7,483**	**20,357**	**32,471**	**(16,026)**	**16,445**	**10,467**
A/A2	**13,422**	**26,550**	**42,797**	**82,769**	**(57,868)**	**24,901**	**16,326**
BBB/Baa2	**7,032**	**12,173**	**27,676**	**46,881**	**(32,962)**	**13,919**	**4,577**
BB/Ba2 or lower	**2,489**	**5,762**	**7,676**	**15,927**	**(9,116)**	**6,811**	**4,544**
Unrated	**326**	**927**	**358**	**1,611**	**(13)**	**1,598**	**1,259**
Total	**$28,394**	**$54,829**	**$101,642**	**$184,865**	**$(117,461)**	**$67,404**	**$40,616**

in millions	As of December 2011						
Credit Rating Equivalent	0 - 12 Months	1 - 5 Years	5 Years or Greater	Total	Netting	Exposure	Exposure Net of Collateral
AAA/Aaa	$ 727	$ 786	$ 2,297	$ 3,810	$ (729)	$ 3,081	$ 2,770
AA/Aa2	4,661	10,198	28,094	42,953	(22,972)	19,981	12,954
A/A2	17,704	36,553	50,787	105,044	(73,873)	31,171	17,109
BBB/Baa2	7,376	14,222	25,612	47,210	(36,214)	10,996	6,895
BB/Ba2 or lower	2,896	4,497	6,597	13,990	(6,729)	7,261	4,527
Unrated	752	664	391	1,807	(149)	1,658	1,064
Total	$34,116	$66,920	$113,778	$214,814	$(140,666)	$74,148	$45,319

Lending Activities. We manage the firm's traditional credit origination activities, including funded loans and lending commitments (both fair value and held for investment loans and lending commitments), using the credit risk process, measures and limits described above. Other lending positions, including secondary trading positions, are risk-managed as a component of market risk.

Other Credit Exposures. The firm is exposed to credit risk from its receivables from brokers, dealers and clearing organizations and customers and counterparties. Receivables from brokers, dealers and clearing organizations are primarily comprised of initial margin placed with clearing organizations and receivables related to sales of securities which have traded, but not yet settled. These receivables have minimal credit risk due to the low probability of clearing organization default and the short-term nature of receivables related to securities settlements. Receivables from customers and counterparties are generally comprised of collateralized receivables related to customer securities transactions and have minimal credit risk due to both the value of the collateral received and the short-term nature of these receivables.

Credit Exposures

As of December 2012, our credit exposures increased as compared with December 2011, reflecting an increase in cash and loans and lending commitments, partially offset by a decrease in OTC derivative exposures. The percentage of our credit exposure arising from non-investment-grade counterparties (based on our internally determined public rating agency equivalents) increased from December 2011 reflecting an increase in loans and lending commitments. Counterparty defaults rose slightly during the year ended December 2012; however, the estimated losses associated with these counterparty defaults were lower as compared with the prior year.

The tables below present the firm's credit exposures related to cash, OTC derivatives, and loans and lending commitments associated with traditional credit origination activities broken down by industry, region and internal credit rating.

Credit Exposure by Industry

in millions	Cash		OTC Derivatives		Loans and Lending Commitments [1]	
	As of December		As of December		As of December	
	2012	2011	**2012**	2011	**2012**	2011
Asset Managers & Funds	**$ —**	$ 64	**$10,552**	$10,582	**$ 1,673**	$ 1,290
Banks, Brokers & Other Financial Institutions	**10,507**	12,535	**21,310**	25,041	**6,192**	3,591
Consumer Products, Non-Durables & Retail	**—**	11	**1,516**	1,031	**13,304**	12,685
Government & Central Banks	**62,162**	43,389	**14,729**	16,642	**1,782**	1,828
Healthcare & Education	**—**	—	**3,764**	2,962	**7,717**	7,158
Insurance	**—**	—	**4,214**	2,828	**3,199**	2,891
Natural Resources & Utilities	**—**	—	**4,383**	4,803	**16,360**	14,795
Real Estate	**—**	—	**381**	327	**3,796**	2,695
Technology, Media, Telecommunications & Services	**—**	2	**2,016**	2,124	**17,674**	12,646
Transportation	**—**	—	**1,207**	1,104	**6,557**	5,753
Other	**—**	7	**3,332**	6,704	**4,650**	5,759
Total [2]	**$72,669**	$56,008	**$67,404**	$74,148	**$82,904**	$71,091

Credit Exposure by Region

in millions	Cash		OTC Derivatives		Loans and Lending Commitments [1]	
	As of December		As of December		As of December	
	2012	2011	**2012**	2011	**2012**	2011
Americas	**$65,193**	$48,543	**$32,968**	$36,591	**$59,792**	$52,755
EMEA [3]	**1,683**	1,800	**26,739**	29,549	**21,104**	16,989
Asia	**5,793**	5,665	**7,697**	8,008	**2,008**	1,347
Total [2]	**$72,669**	$56,008	**$67,404**	$74,148	**$82,904**	$71,091

Credit Exposure by Credit Quality

in millions **Credit Rating Equivalent**	Cash		OTC Derivatives		Loans and Lending Commitments [1]	
	As of December		As of December		As of December	
	2012	2011	**2012**	2011	**2012**	2011
AAA/Aaa	**$59,825**	$40,559	**$ 3,730**	$ 3,081	**$ 2,179**	$ 2,192
AA/Aa2	**6,356**	7,463	**16,445**	19,981	**7,220**	7,026
A/A2	**5,068**	6,464	**24,901**	31,171	**21,901**	21,055
BBB/Baa2	**326**	195	**13,919**	10,996	**26,313**	22,937
BB/Ba2 or lower	**1,094**	1,209	**6,811**	7,261	**25,291**	17,820
Unrated	**—**	118	**1,598**	1,658	**—**	61
Total [2]	**$72,669**	$56,008	**$67,404**	$74,148	**$82,904**	$71,091

1. Includes approximately $12 billion and $10 billion of loans as of December 2012 and December 2011, respectively, and approximately $71 billion and $61 billion of lending commitments as of December 2012 and December 2011, respectively. Excludes certain bank loans and bridge loans and certain lending commitments that are risk managed as part of market risk using VaR and sensitivity measures.

2. The firm bears credit risk related to resale agreements and securities borrowed only to the extent that cash advanced or the value of securities pledged or delivered to the counterparty exceeds the value of the collateral received. The firm also has credit exposure on repurchase agreements and securities loaned to the extent that the value of securities pledged or delivered to the counterparty for these transactions exceeds the amount of cash or collateral received. We had approximately $37 billion and $41 billion as of December 2012 and December 2011, respectively, in credit exposure related to securities financing transactions reflecting applicable netting agreements and collateral.

3. EMEA (Europe, Middle East and Africa).

Selected Country Exposures

During 2011 and throughout 2012, there have been concerns about European sovereign debt risk and its impact on the European banking system and a number of European member states have been experiencing significant credit deterioration. The most pronounced market concerns relate to Greece, Ireland, Italy, Portugal and Spain. The tables below present our credit exposure (both gross and net of hedges) to all sovereigns, financial institutions and corporate counterparties or borrowers in these countries. Credit exposure represents the potential for loss due to the default or deterioration in credit quality of a counterparty or borrower. In addition, the tables include the market exposure of our long and short inventory for which the issuer or underlier is located in these countries. Market exposure represents the potential for loss in value of our inventory due to changes in market prices. There is no overlap between the credit and market exposures in the tables below.

The country of risk is determined by the location of the counterparty, issuer or underlier's assets, where they generate revenue, the country in which they are headquartered, and/or the government whose policies affect their ability to repay their obligations.

	As of December 2012											
	Credit Exposure								Market Exposure			
in millions	Loans	OTC Derivatives	Other	Gross Funded	Hedges	Total Net Funded Credit Exposure	Unfunded Credit Exposure	Total Credit Exposure	Debt	Equities and Other	Credit Derivatives	Total Market Exposure
Greece												
Sovereign	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 30	$ —	$ —	$ 30
Non-Sovereign	—	5	1	6	—	6	—	6	65	15	(5)	75
Total Greece	—	5	1	6	—	6	—	6	95	15	(5)	105
Ireland												
Sovereign	—	1	103	104	—	104	—	104	8	—	(150)	(142)
Non-Sovereign	—	126	36	162	—	162	—	162	801	74	155	1,030
Total Ireland	—	127	139	266	—	266	—	266	809	74	5	888
Italy												
Sovereign	—	1,756	1	1,757	(1,714)	43	—	43	(415)	—	(603)	(1,018)
Non-Sovereign	43	560	129	732	(33)	699	587	1,286	434	65	(996)	(497)
Total Italy	43	2,316	130	2,489	(1,747)	742	587	1,329	19	65	(1,599)	(1,515)
Portugal												
Sovereign	—	141	61	202	—	202	—	202	155	—	(226)	(71)
Non-Sovereign	—	44	2	46	—	46	—	46	168	(6)	(133)	29
Total Portugal	—	185	63	248	—	248	—	248	323	(6)	(359)	(42)
Spain												
Sovereign	—	75	—	75	—	75	—	75	986	—	(268)	718
Non-Sovereign	1,048	259	23	1,330	(95)	1,235	733	1,968	1,268	83	(186)	1,165
Total Spain	1,048	334	23	1,405	(95)	1,310	733	2,043	2,254	83	(454)	1,883
Subtotal	$1,091 [1]	$2,967 [2]	$356	$4,414	$(1,842) [3]	$2,572	$1,320	$3,892	$3,500	$231	$(2,412) [3]	$ 1,319

1. Principally consists of collateralized loans.

2. Includes the benefit of $6.6 billion of cash and U.S. Treasury securities collateral and excludes non-U.S. government and agency obligations and corporate securities collateral of $357 million.

3. Includes written and purchased credit derivative notionals reduced by the fair values of such credit derivatives.

in millions	Loans	OTC Derivatives	Other	Gross Funded	Hedges	Total Net Funded Credit Exposure	Unfunded Credit Exposure	Total Credit Exposure	Debt	Equities and Other	Credit Derivatives	Total Market Exposure
	As of December 2011											
	Credit Exposure								Market Exposure			
Greece												
Sovereign	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 329	$ —	$ (22)	$ 307
Non-Sovereign	20	53	—	73	—	73	—	73	32	11	18	61
Total Greece	20	53	—	73	—	73	—	73	361	11	(4)	368
Ireland												
Sovereign	—	1	256	257	—	257	—	257	411	—	(352)	59
Non-Sovereign	—	542	66	608	(8)	600	57	657	412	85	115	612
Total Ireland	—	543	322	865	(8)	857	57	914	823	85	(237)	671
Italy												
Sovereign	—	1,666	3	1,669	(1,410)	259	—	259	210	—	200	410
Non-Sovereign	126	457	—	583	(25)	558	408	966	190	297	(896)	(409)
Total Italy	126	2,123	3	2,252	(1,435)	817	408	1,225	400	297	(696)	1
Portugal												
Sovereign	—	151	—	151	—	151	—	151	(98)	—	23	(75)
Non-Sovereign	—	53	2	55	—	55	—	55	230	13	(179)	64
Total Portugal	—	204	2	206	—	206	—	206	132	13	(156)	(11)
Spain												
Sovereign	—	88	—	88	—	88	—	88	151	—	(550)	(399)
Non-Sovereign	153	254	11	418	(141)	277	146	423	345	239	(629)	(45)
Total Spain	153	342	11	506	(141)	365	146	511	496	239	(1,179)	(444)
Subtotal	$299	$3,265 [1]	$338	$3,902	$(1,584)	$2,318	$611	$2,929	$2,212	$645	$(2,272) [2]	$ 585

1. Includes the benefit of $6.5 billion of cash and U.S. Treasury securities collateral and excludes non-U.S. government and agency obligations and corporate securities collateral of $341 million.

2. Includes written and purchased credit derivative notionals reduced by the fair values of such credit derivatives.

We economically hedge our exposure to written credit derivatives by entering into offsetting purchased credit derivatives with identical underlyings. Where possible, we endeavor to match the tenor and credit default terms of such hedges to that of our written credit derivatives. Substantially all purchased credit derivatives included above are bought from investment-grade counterparties domiciled outside of these countries and are collateralized with cash or U.S. Treasury securities. The gross purchased and written credit derivative notionals across the above countries for single-name and index credit default swaps (included in 'Hedges' and 'Credit Derivatives' in the tables above) were $179.4 billion and $168.6 billion, respectively, as of December 2012, and $177.8 billion and $167.3 billion, respectively, as of December 2011. Including netting under legally enforceable netting agreements, within each and across all of the countries above, the purchased and written credit derivative notionals for single-name and index credit default swaps were $26.0 billion and $15.3 billion, respectively, as of December 2012, and $28.2 billion and $17.7 billion, respectively, as of December 2011. These notionals are not representative of our exposure because they exclude available netting under legally enforceable netting agreements on other derivatives outside of these countries and collateral received or posted under credit support agreements.

In credit exposure above, 'Other' principally consists of deposits, secured lending transactions and other secured receivables, net of applicable collateral. As of December 2012 and December 2011, $4.8 billion and $7.0 billion, respectively, of secured lending transactions and other secured receivables were fully collateralized.

For information about the nature of or payout under trigger events related to written and purchased credit protection contracts see Note 7 to the consolidated financial statements.

We conduct stress tests intended to estimate the direct and indirect impact that might result from a variety of possible events involving the above countries, including sovereign defaults and the exit of one or more countries from the Euro area. In the stress tests, described in "Market Risk Management — Stress Testing" and "Credit Risk Management — Stress Tests/Scenario Analysis," we estimate the direct impact of the event on our credit and market exposures resulting from shocks to risk factors including, but not limited to, currency rates, interest rates, and equity prices. The parameters of these shocks vary based on the scenario reflected in each stress test. We also estimate the indirect impact on our exposures arising from potential market moves in response to the event, such as the impact of credit market deterioration on corporate borrowers and counterparties along with the shocks to the risk factors described above. We review estimated losses produced by the stress tests in order to understand their magnitude, highlight potential loss concentrations, and assess and mitigate our exposures where necessary.

Euro area exit scenarios include analysis of the impacts on exposure that might result from the redenomination of assets in the exiting country or countries. Constructing stress tests for these scenarios requires many assumptions about how exposures might be directly impacted and how resulting secondary market moves would indirectly impact such exposures. Given the multiple parameters involved in such scenarios, losses from such events are inherently difficult to quantify and may materially differ from our estimates. In order to prepare for any market disruption that might result from a Euro area exit, we test our operational and risk management readiness and capability to respond to a redenomination event.

See "Liquidity Risk Management — Modeled Liquidity Outflow," "Market Risk Management — Stress Testing" and "Credit Risk Management — Stress Tests/Scenario Analysis" for further discussion.

Operational Risk Management

Overview

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Our exposure to operational risk arises from routine processing errors as well as extraordinary incidents, such as major systems failures. Potential types of loss events related to internal and external operational risk include:

- clients, products and business practices;
- execution, delivery and process management;
- business disruption and system failures;
- employment practices and workplace safety;
- damage to physical assets;
- internal fraud; and
- external fraud.

The firm maintains a comprehensive control framework designed to provide a well-controlled environment to minimize operational risks. The Firmwide Operational Risk Committee, along with the support of regional or entity-specific working groups or committees, provides oversight of the ongoing development and implementation of our operational risk policies and framework. Our Operational Risk Management department (Operational Risk Management) is a risk management function independent of our revenue-producing units, reports to the firm's chief risk officer, and is responsible for developing and implementing policies, methodologies and a formalized framework for operational risk management with the goal of minimizing our exposure to operational risk.

Operational Risk Management Process

Managing operational risk requires timely and accurate information as well as a strong control culture. We seek to manage our operational risk through:

- the training, supervision and development of our people;
- the active participation of senior management in identifying and mitigating key operational risks across the firm;
- independent control and support functions that monitor operational risk on a daily basis and have instituted extensive policies and procedures and implemented controls designed to prevent the occurrence of operational risk events;
- proactive communication between our revenue-producing units and our independent control and support functions; and
- a network of systems throughout the firm to facilitate the collection of data used to analyze and assess our operational risk exposure.

We combine top-down and bottom-up approaches to manage and measure operational risk. From a top-down perspective, the firm's senior management assesses firmwide and business level operational risk profiles. From a bottom-up perspective, revenue-producing units and independent control and support functions are responsible for risk management on a day-to-day basis, including identifying, mitigating, and escalating operational risks to senior management.

Our operational risk framework is in part designed to comply with the operational risk measurement rules under Basel 2 and has evolved based on the changing needs of our businesses and regulatory guidance. Our framework comprises the following practices:

- Risk identification and reporting;
- Risk measurement; and
- Risk monitoring.

Internal Audit performs a review of our operational risk framework, including our key controls, processes and applications, on an annual basis to assess the effectiveness of our framework.

Risk Identification and Reporting

The core of our operational risk management framework is risk identification and reporting. We have a comprehensive data collection process, including firmwide policies and procedures, for operational risk events.

We have established policies that require managers in our revenue-producing units and our independent control and support functions to escalate operational risk events. When operational risk events are identified, our policies require that the events be documented and analyzed to determine whether changes are required in the firm's systems and/or processes to further mitigate the risk of future events.

In addition, our firmwide systems capture internal operational risk event data, key metrics such as transaction volumes, and statistical information such as performance trends. We use an internally-developed operational risk management application to aggregate and organize this information. Managers from both revenue-producing units and independent control and support functions analyze the information to evaluate operational risk exposures and identify businesses, activities or products with heightened levels of operational risk. We also provide periodic operational risk reports to senior management, risk committees and the Board.

Risk Measurement

We measure the firm's operational risk exposure over a twelve-month time horizon using both statistical modeling and scenario analyses, which involve qualitative assessments of the potential frequency and extent of potential operational risk losses, for each of the firm's businesses. Operational risk measurement incorporates qualitative and quantitative assessments of factors including:

- internal and external operational risk event data;
- assessments of the firm's internal controls;
- evaluations of the complexity of the firm's business activities;
- the degree of and potential for automation in the firm's processes;
- new product information;
- the legal and regulatory environment;
- changes in the markets for the firm's products and services, including the diversity and sophistication of the firm's customers and counterparties; and
- the liquidity of the capital markets and the reliability of the infrastructure that supports the capital markets.

The results from these scenario analyses are used to monitor changes in operational risk and to determine business lines that may have heightened exposure to operational risk. These analyses ultimately are used in the determination of the appropriate level of operational risk capital to hold.

Risk Monitoring

We evaluate changes in the operational risk profile of the firm and its businesses, including changes in business mix or jurisdictions in which the firm operates, by monitoring the factors noted above at a firmwide level. The firm has both detective and preventive internal controls, which are designed to reduce the frequency and severity of operational risk losses and the probability of operational risk events. We monitor the results of assessments and independent internal audits of these internal controls.

Recent Accounting Developments

See Note 3 to the consolidated financial statements for information about Recent Accounting Developments.

Certain Risk Factors That May Affect Our Businesses

We face a variety of risks that are substantial and inherent in our businesses, including market, liquidity, credit, operational, legal, regulatory and reputational risks. For a discussion of how management seeks to manage some of these risks, see "Overview and Structure of Risk Management." A summary of the more important factors that could affect our businesses follows. For a further discussion of these and other important factors that could affect our businesses, financial condition, results of operations, cash flows and liquidity, see "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K.

- Our businesses have been and may continue to be adversely affected by conditions in the global financial markets and economic conditions generally.
- Our businesses have been and may be adversely affected by declining asset values. This is particularly true for those businesses in which we have net "long" positions, receive fees based on the value of assets managed, or receive or post collateral.
- Our businesses have been and may be adversely affected by disruptions in the credit markets, including reduced access to credit and higher costs of obtaining credit.
- Our market-making activities have been and may be affected by changes in the levels of market volatility.
- Our investment banking, client execution and investment management businesses have been adversely affected and may continue to be adversely affected by market uncertainty or lack of confidence among investors and CEOs due to general declines in economic activity and other unfavorable economic, geopolitical or market conditions.
- Our investment management business may be affected by the poor investment performance of our investment products.
- We may incur losses as a result of ineffective risk management processes and strategies.
- Our liquidity, profitability and businesses may be adversely affected by an inability to access the debt capital markets or to sell assets or by a reduction in our credit ratings or by an increase in our credit spreads.
- Conflicts of interest are increasing and a failure to appropriately identify and address conflicts of interest could adversely affect our businesses.
- Group Inc. is a holding company and is dependent for liquidity on payments from its subsidiaries, many of which are subject to restrictions.
- Our businesses, profitability and liquidity may be adversely affected by deterioration in the credit quality of, or defaults by, third parties who owe us money, securities or other assets or whose securities or obligations we hold.
- Concentration of risk increases the potential for significant losses in our market-making, underwriting, investing and lending activities.
- The financial services industry is highly competitive.
- We face enhanced risks as new business initiatives lead us to transact with a broader array of clients and counterparties and expose us to new asset classes and new markets.
- Derivative transactions and delayed settlements may expose us to unexpected risk and potential losses.
- Our businesses may be adversely affected if we are unable to hire and retain qualified employees.
- Our businesses and those of our clients are subject to extensive and pervasive regulation around the world.
- We may be adversely affected by increased governmental and regulatory scrutiny or negative publicity.
- A failure in our operational systems or infrastructure, or those of third parties, could impair our liquidity, disrupt our businesses, result in the disclosure of confidential information, damage our reputation and cause losses.
- Substantial legal liability or significant regulatory action against us could have material adverse financial effects or cause us significant reputational harm, which in turn could seriously harm our business prospects.
- The growth of electronic trading and the introduction of new trading technology may adversely affect our business and may increase competition.
- Our commodities activities, particularly our power generation interests and our physical commodities activities, subject us to extensive regulation, potential catastrophic events and environmental, reputational and other risks that may expose us to significant liabilities and costs.
- In conducting our businesses around the world, we are subject to political, economic, legal, operational and other risks that are inherent in operating in many countries.
- We may incur losses as a result of unforeseen or catastrophic events, including the emergence of a pandemic, terrorist attacks, extreme weather events or other natural disasters.