

SMBC CAPITAL MARKETS, INC.
(A Wholly Owned Subsidiary of
SMBC Americas Holdings, Inc.)

Statement of Financial Condition

December 31, 2021

(With Independent Auditors' Report Thereon)

SMBC CAPITAL MARKETS, INC.
(A Wholly Owned Subsidiary of
SMBC Americas Holdings, Inc.)

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KPMG LLP
345 Park Avenue
New York, NY 10154-0102

Independent Auditors' Report

To the Board of Directors and Stockholder
SMBC Capital Markets, Inc.:

Opinion

We have audited the statement of financial condition of SMBC Capital Markets, Inc. (the Company) as of December 31, 2021, and the related notes to the financial statement.

In our opinion, the accompanying financial statement presents fairly, in all material respects, the financial position of the Company as of December 31, 2021, in accordance with U.S. generally accepted accounting principles.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statement section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statement

Management is responsible for the preparation and fair presentation of the financial statement in accordance with U.S. generally accepted accounting principles, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statement, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for one year after the date that the financial statement is available to be issued.

Auditors' Responsibilities for the Audit of the Financial Statement

Our objectives are to obtain reasonable assurance about whether the financial statement as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statement.



In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statement, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statement.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statement.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

KPMG LLP

New York, New York
February 28, 2022

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Assets	
Cash and cash equivalents, and restricted cash	\$ 471,554,050
Cash collateral pledged	529,760,788
Derivative assets, net, at fair value	2,037,544,091
Securities purchased under agreements to resell	1,341,202,037
Trading assets, net, at fair value (includes \$268,925,120 pledged as collateral)	948,661,229
Due from brokers	161,530,966
Leveraged leases	82,390,623
Investment in affiliate	200,000,000
Investment in limited partnership	3,949,475
Income taxes receivable, net	8,950,591
Other assets	151,681,374
Total assets	<u>\$ 5,937,225,224</u>
Liabilities and Stockholder's Equity	
Liabilities:	
Due to banks	\$ 113,559,115
Cash collateral received	323,868,170
Derivative liabilities, net, at fair value	1,389,686,907
Securities sold under agreements to repurchase	293,480,880
Trading liabilities, net, at fair value	769,479,604
Due to brokers	131,195,572
Borrowings from affiliates	1,110,915,963
Income taxes payable, net	23,855,958
Deferred tax liabilities, net	9,033,764
Other liabilities	46,851,975
Total liabilities	<u>4,211,927,908</u>
Commitments and contingencies (see notes 2(j) and 11)	
Stockholder's equity:	
Common stock – Class A, \$0.10 par value. Authorized 50 shares; issued and outstanding - 5 shares	1
Common stock – Class B, \$0.10 par value. Authorized 9,950 shares; issued and outstanding - 995 shares	100
Additional paid-in capital	701,019,067
Retained earnings	1,024,327,358
Accumulated other comprehensive loss	(49,210)
Total stockholder's equity	<u>1,725,297,316</u>
Total liabilities and stockholder's equity	<u>\$ 5,937,225,224</u>

See accompanying notes to statement of financial condition.

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(1) Organization

SMBC Capital Markets, Inc. (“the Company”) was incorporated in the State of Delaware on December 4, 1986, to engage in a wide range of capital market activities. The principal trading activities of the Company include trading in interest rate swaps and options and foreign exchange (FX) products. The Company also engages in certain investment activities, including leveraged lease transactions and other investments.

SMBC Capital Markets Group (“CMG”) conducts derivative marketing and trading activities globally through offices in New York, London and Hong Kong through four legal entities: the Company, SMBC Nikko Capital Markets Limited (“SMBC CM Ltd.”), SMBC Derivative Products Limited (“SMBC DP”) and SMBC CM Asia. The CMG entities market and trade derivative products on an integrated basis and support functions for CMG.

In order to be in compliance with the mandatory regulations under the Dodd-Frank Act effective March 11, 2013, the Company became a clearing member of London Clearing House Clearent Limited (“LCH”) on October 29, 2012 for eligible swaps. On June 18, 2013, the Company entered into an affiliate pass through agreement with SMBC CM Ltd. whereby the Company clears over the counter (OTC) derivative transactions on behalf of SMBC CM Ltd.

The Company is provisionally registered as a swap dealer with the Commodity Futures Trading Commission (“CFTC”) and is also a member of the National Futures Association.

SMBC Americas Holdings, Inc. (“the Parent”), a wholly owned U.S. subsidiary of Sumitomo Mitsui Banking Corporation (“SMBC”), is the sole shareholder of the Company, owning all Class A and Class B shares of the Company’s common stock. Class A and Class B shares entitle the Parent to 100 and 0.5025126 votes per share, respectively. At December 31, 2021, 5 shares of Class A common stock and 995 shares of Class B common stock were outstanding.

(2) Significant Accounting Policies

(a) Basis of Accounting and Use of Estimates

The Company’s statement of financial condition has been prepared in conformity with U.S. generally accepted accounting principles (U.S. GAAP), which requires management to make estimates and assumptions that affect the amounts reported in the statement of financial condition and accompanying notes. Although these, and other, estimates and assumptions are based on the best available information, actual results could be materially different from these estimates. Significant items subject to such estimates and assumptions include the valuation of derivatives, realization of deferred tax assets, income tax uncertainties, other contingencies, and valuation of trading assets and trading liabilities.

(b) Principles of Consolidation

A controlling financial interest may also be achieved through arrangements that do not involve voting interests which are generally obtained through stock ownership. Therefore, the Company evaluates entities for consolidation under the variable interest entity (“VIE”) model in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 810, *Consolidation*. A VIE is an entity that has either a total equity investment that is insufficient to finance its activities without additional subordinated financial support or whose equity investors lack the ability to control the entity’s activities or lack the ability to receive expected benefits or absorb obligations in a manner that’s consistent with their investment in the entity. A VIE is consolidated by its primary beneficiary, the party that has both the power to direct the activities that most significantly impact the VIE’s

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economic performance and a variable interest (obligation to absorb losses from or the right to receive benefits of the VIE) that could potentially be significant to the VIE. A variable interest is a contractual, ownership or other interest that fluctuates with changes in the fair value of the VIE's net assets. To determine whether or not a variable interest the Company holds could potentially be significant to the VIE, the Company considers both qualitative and quantitative factors regarding the nature, size and form of the Company's involvement with the VIE. The Company had no variable interests in a VIE that required consolidation at December 31, 2021.

(c) Foreign Currencies

(i) Translation

Assets and liabilities from the Company's limited partnership investment accounted for under the equity method that are denominated in non U.S. dollar currencies are translated into U.S. dollar equivalents using spot FX rates.

(ii) Transaction

Other assets and liabilities denominated in non-U.S. dollar currencies are remeasured into U.S. dollar equivalents using year-end adjusted spot FX rates.

(d) Cash and Cash Equivalents, and Restricted Cash

The Company considers all highly liquid financial instruments with original maturities of three months or less to be cash equivalents. As of December 31, 2021, cash and cash equivalents and accrued interest receivable was \$396,054,050 and \$9,155 (included in other assets), respectively

Restricted cash is cash that is considered legally restricted as to withdrawal or usage. The following table provides a reconciliation of cash and cash equivalents, and restricted cash reported within the statement of financial condition, that sum to the total of the same such amounts shown in the statement of cash flows as of December 31, 2021:

Cash and cash equivalents	\$ 396,054,050
Restricted cash	75,500,000
Total cash and cash equivalents, and restricted cash shown in the statement of cash flows	<u>\$ 471,554,050</u>

Amount shown in restricted cash represents those required to be set aside by a contractual agreement.

Refer to note 8(a) for further information on cash and cash equivalents.

(e) Cash Collateral Pledged and Received

The Company enters into derivative transactions with counterparties, which may be subject to bilateral collateral agreements. The Company monitors the fair value of its derivative transactions on a daily basis, with additional collateral obtained or refunded as necessary. Additionally, the Company nets the fair value of cash collateral pledged or received against the fair value amounts recognized for net derivative positions pursuant to enforceable master netting agreements. Independent amounts ("IA") represents collateral required over and above the mark to market of a portfolio to provide an additional buffer of protection for certain risk.

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LCH Clearnet, Chicago Mercantile Exchange, and ICE Clear Credit made changes to their rulebook, pursuant to the CFTC interpretation letter 17-51 which confirmed that variation margin and all other payments on a counterparty's cleared swap positions are settled to market (STM) and not collateralized to market (CTM). Therefore, the fair value of derivatives and valuation margin are combined as one unit of accounting for these counterparties, respectively.

As of December 31, 2021, the Company had pledged cash collateral, inclusive of IA pledged, of \$3,049,302,067 gross at fair value, of which \$242,898 was accrued interest receivable.

As of December 31, 2021, the Company had received cash collateral, inclusive of IA received, of \$4,037,173,411 gross at fair value, of which \$395,688 was accrued interest payable.

Refer to notes 3, 8(b) for further information on cash collateral.

(f) Derivative Financial Instruments

Derivative financial instruments consist of interest rate swaps and options and FX products which are recorded at fair value in the accompanying statement of financial condition. The fair values recorded take into consideration market, liquidity, credit, and funding risks. The Company uses the fair value portfolio exception to measure its derivative portfolio since it manages its derivatives portfolio on the basis of its net exposure to these risks. The Company accounts for derivative financial instruments in accordance with FASB ASC 815, *Derivatives and Hedging*.

In addition to trading activities, the Company enters into various derivative contracts as an end-user to economically hedge and/or modify its exposure to the FX and interest rate risk of certain assets and liabilities. A summary of the derivatives portfolio is as follows:

(i) Foreign Exchange Contracts

The Company is involved in a variety of FX forward, futures, swap, and option contracts in its trading activities. The parties to a currency swap initially exchange a principal amount in two currencies, agreeing to re-exchange the currencies at a future date and an agreed-upon exchange rate. Futures contracts are traded on exchanges, reducing the credit risk as compared with deals with other counterparties in over-the-counter markets.

Currency options, which are either exchange-traded or directly negotiated, provide the holder with the right to buy from or sell to the writer an agreed amount of currency at a specified exchange rate within a stated period. The Company's FX contracts primarily relate to major foreign currencies such as the Japanese yen, the Canadian dollar, the British pound, and the Euro.

(ii) Interest Rate Contracts

Interest rate swaps are one of the primary derivative instruments used by the Company in its trading activities. The two parties to an interest rate swap agree to exchange, at particular intervals, payment streams calculated on a specified notional amount, with at least one stream based on a floating interest rate. Basis swaps involve floating rates, such as the prime rate, the London Interbank Offered Rate ("LIBOR"), Overnight Indexed Swap ("OIS") rate, Sterling Overnight Index Average (SONIA), Euro Interbank Offered Rate (EONIA) and the Secured Overnight Financing Rate ("SOFR").

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Interest rate forward and futures contracts are commitments to either purchase or sell a financial instrument at a future date for a specified price and may be settled in cash or through delivery of the underlying financial instrument. Forward rate agreements settle in cash at a specified future date based on the differential between agreed interest rates and an index applied to a notional amount.

Interest rate options grant the purchaser, for a premium payment, the right to either purchase from or sell to the writer a specified financial instrument under agreed-upon terms. Interest rate caps and floors require the writer to pay the purchaser at specified future dates the amount, if any, by which a specified market interest rate exceeds the fixed cap rate or falls below the fixed floor rate, applied to a notional amount. The option, cap, or floor writer receives a premium for bearing the risk of unfavorable interest rate changes.

(iii) Other Contracts

Other contracts include credit derivatives.

Refer to notes 3 and 7(a) for further information on derivative financial instruments.

(g) Securities Purchased under Agreements to Resell and Securities Sold under Agreements to Repurchase

Securities purchased under agreements to resell (reverse repurchase agreements) and securities sold under agreements to repurchase (repurchase agreements) are treated as financing transactions and are carried at amounts at which the securities will be subsequently resold or repurchased, inclusive of accrued interest. The agreements obligate the transferor to repurchase or redeem the same or substantially the same assets before maturity at a fixed or determinable price and the agreements are entered in contemplation of the transfer.

As of December 31, 2021, the Company had securities purchased under agreements to resell of \$1,341,202,037 and securities sold under agreements to repurchase of \$293,480,880.

As of December 31, 2021, the Company pledged securities for repurchase agreements with a fair value of \$293,811,099 and received securities for reverse repurchase agreements with a fair value of \$1,338,032,214. As of December 31, 2021, the Company had the right to sell and sold all of the securities it has received under its reverse repurchase agreements. All securities collateral received from counterparties consisted of government securities. Additional collateral is requested when market value of the securities received decline below the principal amount lent plus accrued interest. Securities pledged or received and subsequently sold under repurchase agreements are not offset and are presented within trading assets and liabilities, at fair value, respectively, on the statement of financial condition.

Refer to notes 3, 4, 7(c) and 8(d) for further information on securities purchased under agreements to resell and securities sold under agreements to repurchase.

(h) Trading Assets and Liabilities

Trading assets at December 31, 2021 include U.S. government securities, foreign government securities, and certain other fixed income financial instruments. Securities are primarily bought and held for the purpose of selling in the near term. Certain securities are held and pledged as collateral against derivative transactions covered by Collateral Agreements. If the Collateral Agreements allow the counterparty to repledge the Company's proprietary securities

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posted, the Company will disclose these securities as securities pledged to counterparties, as applicable. Refer to note 3 for further information.

Securities included in trading assets and trading liabilities are recorded at fair market value on a trade-date basis.

Fixed income financial instruments included in trading assets and trading liabilities represent contractual agreements with counterparties that provide fixed or variable periodic payments from a stated or contingent date over a specified time period. The Company records these fixed income financial instruments at fair value.

Refer to notes 3, 7(b) and 8(e) for further information on trading assets and liabilities.

(i) Fixed Assets and Internal Use Software

Fixed assets, consisting of equipment and leasehold improvements along with internal use software are stated at amortized cost. Furniture is depreciated on a straight-line basis over seven years. Equipment and internal use software is amortized on a straight-line basis over five years. Leasehold improvements are amortized over the lesser of their estimated useful lives or the remaining term of the underlying leases. At December 31, 2021, fixed assets and internal use software were \$21,193,916 and \$11,817,086, respectively, and accumulated depreciation and amortization was \$13,717,769 and \$5,742,788, respectively, and are included in other assets in the accompanying statement of financial condition.

(j) Contingencies

Liabilities for loss contingencies arising from claims, assessments, litigation, fines and penalties, and other sources are recorded when it is probable that a liability has been incurred and the amount can be reasonably estimated.

(k) Fair Value of Financial Instruments

The Company's financial instruments are stated at fair value, except for securities purchased under agreements to resell, securities sold under agreements to repurchase, leveraged leases, and loans payable, which are stated at their contract values or amortized cost. The contract values or amortized cost for these financial instruments, with the exception of leveraged leases, are considered to approximate fair value as they are short term in nature, bear interest at current market rates, or are subject to near term re-pricing. Leveraged leases and the limited partnership investments accounted for under the equity method are excluded for a non-public business entity from the scope of the fair value disclosure requirements of FASB ASC 825, *Financial Instruments*.

The fair values of the Company's financial instruments are determined in accordance with ASC 820, *Fair Value Measurements*. ASC 820 defines fair value, establishes a consistent framework for measuring fair value, and requires disclosure about fair value measurements. ASC 820, among other things, requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. In addition, ASC 820 precludes the use of block discounts when measuring the fair value of instruments traded in an active market. It also requires recognition of trade-date gains related to certain derivative transactions whose fair value has been determined using observable market inputs.

ASC 820 specifies a hierarchy of inputs based on whether the inputs are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. In accordance with ASC 820, the following is the fair value hierarchy:

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- Level 1 - Quoted prices for identical instruments in active markets.
- Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.
- Level 3 - Valuations in which one or more significant inputs or significant value drivers are unobservable. Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company's own estimates of assumptions that market participants would use in pricing the asset or liability.

This hierarchy requires the use of observable market data when available.

Refer to note 7 for further information on fair value on financial instruments.

(l) Fair Value Option

Under the Fair Value Option Subsections of FASB ASC Subtopic 825-10, *Financial Instruments – Overall*, the Company has the irrevocable option to report certain financial assets and financial liabilities at fair value on an instrument-by-instrument basis, with changes in fair value reported in earnings. The Company has not applied the option to any asset or liability items.

(m) Income Taxes

Income taxes are accounted for in accordance with ASC 740, *Income Taxes*, under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the statement of financial condition carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A tax liability or asset is also recognized for the estimated taxes payable or refundable on tax returns for the current and prior years. The Company does not offset receivable and payable amounts for current or deferred taxes related to different tax jurisdictions.

The Company evaluates its uncertain tax positions and the related tax reserves in accordance with the framework set out under ASC 740. ASC 740 provides guidelines for both identifying the uncertain tax positions and determining the appropriate level of tax reserves related to those positions. ASC 740 also sets out disclosure requirements to enhance transparency of an entity's tax reserves.

Deferred taxes are recorded for the future consequences of events that have been recognized for financial statements or tax returns, based upon enacted tax laws and rates. Deferred tax assets are recognized subject to management's judgment that realization is more likely than not.

Refer to note 6 for further information on income tax.

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(n) Investment in Limited Partnership

The Company has an investment in Moelis & Company Group LP (“Moelis Group LP”). The investment in Moelis Group LP is accounted for under the equity method of accounting. As of December 31, 2021, the book value of the investment in Moelis Group LP was \$3,949,475.

The Company evaluates if its investment in a limited partnership is other than temporarily impaired (“OTTI”) (1) whenever management has estimated the fair value of the investment to be lower than its carrying book value and (2) whenever an event or change in circumstances occurs that may have a significant adverse impact on the fair value of the investment. As of December 31, 2021, the Company’s investment in Moelis Group was not impaired.

The Company’s policies for assessing if an investment is OTTI include an evaluation of the absence of an ability to recover the carrying amount of the investment within an acceptable forecast period, inability of the investment to sustain an earnings capacity that would justify its carrying amount and the severity and time period of a decline of fair value below book value.

Refer to note 8(g) for further information on the investment in limited partnership.

(o) Employee Compensation and Benefits

The Company pays discretionary cash bonuses to its employees and certain cash bonuses are deferred over a service period of three years. An employee with a deferred bonus earns a portion of the cash bonus in each of the three years if they continue employment at the Company. All deferred cash bonuses have clawback provisions. None of the clawback provisions have been triggered for the year ended December 31, 2021. The deferred compensation liability was \$2,649,617 as of December 31, 2021.

(p) Recent Accounting Developments

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. Topic 842 was subsequently amended by ASU No. 2018-01, *Land Easement Practical Expedient for Transition to Topic 842*; ASU No. 2018-10, *Codification Improvements to Topic 842, Leases*; ASU No. 2018-11, *Leases (Topic 842): Targeted Improvements*, ASU No. 2018-20, *Leases (Topic 842) - Narrow-Scope Improvements for Lessors*, ASU 2019-01, *Leases (Topic 842): Codification Improvements* and ASU No. 2021-09, *Leases (Topic 842): Discount Rate for Lessees That Are Not Public Business Entities*. ASU No. 2016-02 requires that, at lease inception for all leases, a lessee recognize in the statement of financial condition a right-of-use asset, for the right to use the underlying asset over the lease term, and a lease liability, for the liability to make lease payments for all leases with a term longer than 12 months. The classification criteria for distinguishing between finance leases and operating leases are substantially similar to the classification criteria for distinguishing between capital leases and operating leases in the previous lease guidance. Lessor accounting is largely unchanged; however, the leveraged lease model is not retained for leases that commence after the effective date of ASU No. 2016-02. In addition, ASU No. 2016-02 requires expanded disclosures about the nature and terms of lease agreements. Public business entities, certain not for profit entities, and certain employee benefit plans should apply this standard to annual reporting periods beginning after December 15, 2018. In November 2019, the FASB issued ASU No. 2019-10, *Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*. The Board developed a new philosophy to extend and simplify how effective dates are staggered between larger public companies and all other entities. Following the new effective date philosophy, the mandatory effective dates were deferred for *Leases (Topic 842)* for all other entities by an additional year. In April 2020, the FASB issued ASU No. 2020-05—*Revenue from Contracts with*

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Customers (Topic 606) and Leases (Topic 842): Effective Dates for Certain Entities. For leases, the ASU provides an effective date deferral to private companies, private not-for-profit organizations, and public not-for-profit organizations that have not yet issued (or made available) their financial statements reflecting the adoption of the guidance. Under the ASU, private companies and private not-for-profit organizations may apply the new leases standard for fiscal years beginning after December 15, 2021 (January 1, 2022, for calendar-year-end companies). Early adoption will continue to be allowed. Therefore, the Company adopted this guidance on January 1, 2022. The Company used the modified retrospective transition approach, which requires application of the new standard to all leases existing at the date of initial application (which the Company chose as the adoption date, January 1, 2022). The new standard provides a number of optional practical expedients in transition. The Company elected to use the package of practical expedients and applied it consistently to all of its leases, which permits the Company not to reassess under the new standard our prior conclusions about lease identification, lease classification and initial direct costs. The Company did not elect the use-of-hindsight or the practical expedient pertaining to land easements; the latter not being applicable to the Company. The adoption of Topic 842 resulted in both right of use assets and lease liabilities of \$23,146,144 based on the present value of the remaining minimum rental payments under current leasing standards for existing operating leases.

In June 2016, FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Assets*, which is to replace the incurred loss impairment methodology in current U.S. GAAP with a methodology that reflects lifetime expected credit losses and requires consideration of a broader range of reasonable and supportable information to develop credit loss estimates. Specifically, the amendments in this ASU would eliminate the probable initial recognition threshold in current U.S. GAAP and, instead, reflect an entity's current estimate of all expected credit losses. In November 2018, the FASB issued ASU No. 2018-19, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses*. The amendments in this update require that for nonpublic business entities the amendments in ASU No. 2016-13 are effective for fiscal years beginning after December 15, 2021 and clarifies that receivables arising from operating leases are not within the scope of Subtopic 326-20. In April 2019, the FASB issued ASU No. 2019-04, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments*. The amendments related to Topic 326 address the presentation and disclosure of accrued interest balances, that recoveries should be included in the allowance, allow the use of projections of future interest rate environments when using a discounted cash flow method to measure expected credit losses on variable-rate financial instruments and to allow for an adjustment of the effective interest rate used to discount expected future cash flows for expected prepayments on financial assets. In May 2019, the FASB issued ASU No. 2019-05, *Financial Instruments—Credit Losses (Topic 326): Targeted Transition Relief*. The ASU amends the transition guidance in the new credit losses standard and provides entities with an option upon adoption of ASC 326-20, to irrevocably elect the fair value option for certain financial instruments that are both: (a) within the scope of ASC 326-20 and (b) eligible for the fair value option in ASC 825-10, *Financial Instruments—Overall*. This election should be applied on an instrument-by-instrument basis for eligible financial assets. In November 2019, the FASB issued ASU No. 2019-10, *Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*. The Board developed a new philosophy to extend and simplify how effective dates are staggered between larger public companies and all other entities. Following the new effective date philosophy, the mandatory effective dates for Credit Losses in Topic 326 are as follows: 1. Public business entities that meet the definition of an SEC filer, excluding entities eligible to be SRCs as defined by the SEC, for fiscal years beginning after December 15, 2019, 2. All other entities for fiscal years beginning after December 15, 2022. In November 2019, the FASB issued ASU No. 2019-11, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses*. ASU No. 2019-11 provides for several

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amendments. One of the amendments clarifies that an entity should assess whether it reasonably expects the borrower will be able to continually replenish collateral securing the financial asset to apply the collateral maintenance practical expedient. The amendments clarify that an entity applying the practical expedient should estimate expected credit losses for any difference between the amount of the amortized cost basis that is greater than the fair value of the collateral securing the financial asset (that is, the unsecured portion of the amortized cost basis). An entity may determine that the expectation of nonpayment for the amount of the amortized cost basis equal to the fair value of the collateral securing the financial asset is zero. In February 2020, the FASB issued ASU No. 2020-02 *Financial Instruments—Credit Losses (Topic 326) and Leases (Topic 842)*, this ASU adds an SEC paragraph pursuant to the issuance of SEC Staff Accounting Bulletin No. 119 (“SAB 119”). SAB 119 updated the SEC’s guidance in SAB Topic 6.M to conform with the accounting guidelines in ASC Topic 326. A lessor’s net investment in a sales-type or direct financing lease will be in scope of ASC Topic 326 once that standard becomes effective. In February 2020, the FASB issued ASU No. 2020-03, *Codification Improvements to Financial Instruments*, which further amends ASU 2016-13, The ASU makes specific amendments to certain financial instruments guidance including a clarification that the contractual term used to estimate the loss for a net investment in a lease should be the “lease term” ASU No. 2016-13 (Topic 326), as amended by above mentioned ASUs, is effective for entities that are not public business entities for annual periods beginning after December 15, 2022. Therefore, Topic 326 will be effective for the Company on January 1, 2023. The Company is evaluating the effect that ASU No. 2016-13 (Topic 326), will have on the statement of financial condition.

In August 2018, the FASB issued ASU No. 2018-15, *Intangibles – Goodwill and Other – Internal-Use Software (subtopics 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract*, which generally aligns the standard on recognizing implementation costs incurred in a cloud computing arrangement that is a service contract with the standard for implementation costs incurred to develop or obtain internal-use software, including hosting arrangements that include an internal-use software license. Accordingly, the amendments require an entity (customer) in a hosting arrangement that is a service contract to follow the standard in Subtopic 350-40 to determine which implementation costs to capitalize as an asset related to the service contract and which costs to expense. The amendments also require the entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement, which includes reasonably certain renewals. The amendments in ASU 2018-15 are effective for public business entities for fiscal years beginning after December 15, 2019. For all other entities, the amendments in ASU 2018-15 are effective for annual reporting periods beginning after December 15, 2020. Early adoption of the amendments in ASU 2018-15 is permitted for all entities. The amendments in ASU 2018-15 should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. The Company adopted this guidance on January 1, 2021. The adoption of ASU No. 2018-15 did not have an impact on the statement of financial condition of the Company.

In October 2018, the FASB issued ASU No. 2018-17, *Targeted Improvements to Related Party Guidance for Variable Interest Entities*. Under the amendments in ASU 2018-17, a private company (reporting entity) may elect not to apply the VIE guidance to legal entities under common control (including common control leasing arrangements) if both the parent and the legal entity being evaluated for consolidation are not public business entities. The accounting alternative provides an accounting policy election that a private company will apply to all current and future legal entities under common control that meet the criteria for applying this alternative. If the alternative is elected, a private company should continue to apply other consolidation guidance, particularly the voting interest entity guidance, unless another scope exception applies. Also, the amendments in ASU 2018-17 for determining

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whether a decision-making fee is a variable interest require reporting entities to consider indirect interests held through related parties under common control on a proportional basis rather than as the equivalent of a direct interest in its entirety (as currently required in U.S. GAAP). Therefore, these amendments likely will result in more decision makers not having a variable interest through their decision-making arrangements. These amendments also will create alignment between determining whether a decision-making fee is a variable interest and determining whether a reporting entity within a related party group is the primary beneficiary of a VIE. For entities other than private companies, the amendments in ASU 2018-17 are effective for fiscal years beginning after December 15, 2019. The amendments in ASU 2018-17 are effective for private companies for fiscal years beginning after December 15, 2020. All entities are required to apply the amendments in this Update retrospectively with a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented. Early adoption is permitted. The Company adopted this guidance on January 1, 2021. The adoption of ASU No. 2018-17 did not have an impact on the statement of financial condition of the Company.

In December 2018, the FASB issued ASU No. 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*. The amendments in this Update simplify the accounting for income taxes by removing certain exceptions to the general principles in Topic 740. The amendments also improve consistent application of and simplify U.S. GAAP for other areas of Topic 740 by clarifying and amending existing guidance for franchise taxes that are partially based on income, transactions with a government that result in a step up in the tax basis of goodwill, separate financial statements of legal entities that are not subject to tax and enacted changes in tax laws in interim periods. For entities other than private companies, the amendments in ASU 2019-12 are effective for fiscal years beginning after December 15, 2020. The amendments in ASU 2019-12 are effective for private companies for fiscal years beginning after December 15, 2021. Early adoption is permitted. Therefore, the ASU was adopted by the Company on January 1, 2022. The adoption of ASU No. 2019-12 did not have a material impact on the statement of financial condition of the Company.

In March 2020, the FASB issued a new ASU No. 2020-04, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*. This ASU provides temporary optional expedients and exceptions to GAAP guidance on contract modifications and hedge accounting to ease the financial reporting burdens of the expected market transition from LIBOR and other interbank offered rates to alternative reference rates, such as SOFR, SONIA, EONIA. For instance, entities can (1) elect not to apply certain modification accounting requirements to contracts affected by reference rate reform, if certain criteria are met. An entity that makes this election would not have to remeasure the contracts at the modification date or reassess a previous accounting determination; (2) elect various optional expedients that would allow them to continue applying hedge accounting for hedging relationships affected by reference rate reform, if certain criteria are met; and (3) make a one-time election to sell and/or reclassify held-to-maturity debt securities that reference an interest rate affected by reference rate reform. This guidance became effective on March 12, 2020 and an entity may elect to prospectively apply each category of exemption independently in a subsequent period through December 31, 2022. We will implement processes as appropriate to assess the population of contracts that will be impacted by this ASU and to evaluate expedients we will use and when we may apply them. In January 2021, the FASB issued ASU No. 2021-01, *Reference Rate Reform (Topic 848): Scope*. This ASU clarifies that certain optional expedients and exceptions in Topic 848 for contract modifications and hedge accounting apply to derivatives that are affected by the discounting transition. The ASU also amends the expedients and exceptions in Topic 848 to capture the incremental consequences of the scope clarification and to tailor the existing guidance to derivative instruments affected by the discounting transition. The Company adopted ASU No. 2021-01 retrospectively as of July 1, 2020. The Company

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applied certain of the practical expedients in Topic 848 to its derivatives cleared by LCH and CME that were impacted by changes in the interest rate used for margining, discounting, or contract price alignment of derivative instruments as a result of reference rate reform. During 2021, cleared Euro, GBP and JPY trades transitioned to using SOFR and EONIA discounting rates. The Company adopted ASU No. 2020-04 prospectively as of October 1, 2021. As of the date, the contractual reference transition took place at LCH and JSCC during 2021, the net impact on the statement of financial condition was an increase in derivative assets, net, at fair value of \$1,110,833.

(3) Derivative Financial Instruments

As a trader of derivative financial instruments, the Company enters into transactions in financial instruments with off-balance-sheet risk in the normal course of its business. These financial instruments include interest rate and currency swaps, caps, floors, other option products, interest rate and currency futures contracts, and foreign currency forward contracts.

At December 31, 2021, the total notional amounts related to derivative instruments consisted of the following:

	<u>Notional</u>	<u>Maturity</u>
Foreign exchange contracts	\$ 234,212,120,413	2022-2052
Interest rate contracts	5,360,672,612,167	2022-2071
Other contracts	800,000,000	2022-2026

Although the notional amounts identified above may be indicative of the significance of the Company's trading activities in these financial instruments, they do not represent the amounts exchanged by the parties for derivative transactions and do not measure the exposure to credit or market risks, when taken in isolation. The amounts exchanged are based on the notional amounts and other terms of the derivative instrument agreements. The following paragraphs pertain to risks associated with the uses of derivative financial instruments.

The credit risk due to counterparty nonperformance associated with derivative instruments as of a given point in time is typically limited to the amounts reflected in the Company's statement of financial condition. However, this exposure is subject to change with changes in the fair value of the related derivative instruments. The Company monitors the creditworthiness of counterparties to these transactions on an ongoing basis and seeks to limit credit risk (and concentrations of credit risk) through various controls, including its use of credit exposure reporting systems, related credit limits, and master netting agreements. Master netting agreements incorporate rights of set-off that provide for the net settlement of subject contracts with the same counterparty in the event of default. Such limits are based in part upon the Company's review of the financial conditions and credit ratings of its counterparties. The Company's derivatives products business and its other investments and loans are transacted on a worldwide basis with a large and diversified group of counterparties. The Company has provided valuation adjustments against this risk to the extent to which management believes it is exposed and is consistent with the Company's accounting policies.

All trading instruments are subject to market risk, the potential that future changes in market conditions may make an instrument less valuable due to fluctuations in security prices, as well as interest and FX rates. Market risk is directly impacted by the volatility and liquidity in the markets in which the related underlying assets are traded. Exposure to market risk is managed in accordance with limits set by management.

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Liquidity risk is the possibility that the Company may not be able to rapidly adjust the size of its derivative positions in times of high volatility and financial stress at a reasonable cost. The liquidity of derivative products is highly related to the liquidity of the underlying cash instruments. The Company has provided valuation adjustments against this risk to the extent to which management believes it is exposed and is consistent with the Company's accounting policies.

The Company employs a number of methods to control and measure the risks generated by assets and liabilities arising from both trading and risk management activities. The principal method is the establishment of limits by management, which are regularly assessed to ensure their appropriateness given the Company's objectives, strategies, and current market conditions.

The following tables summarize fair value information at December 31, 2021 of derivative financial instruments held or issued by the Company on a gross basis prior to consideration of collateral and netting agreements. It also discloses the gross fair values of the derivatives by type of instrument (i.e., foreign exchange contracts, interest rate contracts and other) and type of counterparty (over-the-counter, cleared and exchange traded), defined below:

- Over-the-counter derivatives include derivatives executed and settled bilaterally with counterparties without the use of an organized exchange or a central clearing house.
- Cleared derivatives include derivatives executed bilaterally with counterparties in the OTC market but then novated to a central clearing house, whereby the central clearing house becomes the counterparty to both of the original counterparties.
- Exchange traded derivatives include derivatives executed directly on an organized exchange.

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	December 31, 2021	
	Fair value derivative assets	Fair value derivative liabilities
Over-the-counter	\$ 4,511,927,225	4,001,081,128
Cleared	—	—
Exchange traded	—	—
Foreign exchange contracts	4,511,927,225	4,001,081,128
Over-the-counter	7,619,798,644	6,809,572,019
Cleared	11,319,215	1,368,642
Exchange traded	644,296,782	132,436,227
Interest rate contracts	8,275,414,641	6,943,376,888
Over-the-counter	230,665	311,199
Cleared	—	1,182,171
Exchange traded	—	—
Other contracts	230,665	1,493,370
Total derivatives, gross amount recognized	12,787,572,531	10,945,951,386
Less cash collateral and counterparty netting	(10,750,028,440)	(9,556,264,479)
Total derivatives, net amount recognized on the statement of financial condition	2,037,544,091	1,389,686,907
Additional amounts subject to a master netting agreement but not offset on the statement of financial condition		
Less:		
Does not meet applicable offsetting guidance	(55,003,789)	(2,614,692)
Noncash collateral received/pledged	(806,390,039)	(533,561,901)
Total derivatives, net amount	\$ 1,176,150,263	853,510,314

Other contracts include credit derivatives purchased, sold and cleared through ICE Clear Credit (a clearing house and central counterparty for credit derivatives) and maturing through to 2026.

All derivatives are reported on the statement of financial condition at fair value. In addition, where applicable, all contracts covered by enforceable master netting agreements are reported net. Gross positive fair values are netted with gross negative fair values by counterparty pursuant to an enforceable master netting agreement. In addition, payables and receivables in respect of cash collateral received from or pledged to a given counterparty are included in this netting.

As of December 31, 2021, \$3,046,687,374 of the gross amount of cash collateral pledged was subject to offset. Of this amount, \$2,519,541,279 was offset against derivative liability positions, and \$527,146,096, was in excess of derivative liability positions and included in cash collateral pledged in the accompanying statement of financial condition. As of December 31, 2021, \$3,982,169,622 of the gross amount of cash collateral received was subject to offset. Of this amount,

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\$3,713,305,241 was offset against derivative asset positions, and \$268,864,381, was in excess of derivative asset positions and included in cash collateral received in the accompanying statement of financial condition.

As of December 31, 2021, the Company pledged variation and initial margin securities with a fair value of \$533,561,901 as collateral and received securities with a fair value of \$806,390,039 under derivative master netting agreements. As of December 31, 2021, the balance of the pledged securities under derivative master netting agreements, includes \$4,929,951 from trading assets, and \$555,158,782 from securities purchased under agreements to resell.

The Company had pledged \$35,997,433 of trading securities with brokers in satisfaction of exchange initial margin requirements. The Company has the right to sell or repledge the securities it has received under derivative master netting agreements, excluding those securities received in satisfaction of initial margin requirements. The fair value of securities received in satisfaction of initial margin requirements include haircuts applied to the different types of securities received based on the margin agreements. Additional collateral is requested when appropriate.

Refer to notes 2(f), 2(k), 7, 8(c) and 10 for more information on derivatives.

(4) Securities Purchased under Agreements to Resell and Securities Sold under Agreements to Repurchase

The Company enters into reverse repurchase agreements and repurchase agreements to accommodate customers' needs and invest the Company's capital. The Company manages credit exposure arising from such transactions by, in appropriate circumstances, entering into master repurchase agreements with counterparties that provide the Company, in the event of counterparty default (such as bankruptcy or a counterparty's failure to pay or perform), the right to net a counterparty's rights and obligations under such agreement and liquidate and offset collateral against the net amount owed by the counterparty. The Company's policy is generally to take possession of securities purchased under agreements to resell, and to receive securities and cash posted as collateral (with rights of re-hypothecation). The following tables present the gross and net, resale and repurchase agreements and the related offsetting amounts as of December 31, 2021.

	<u>Gross amount recognized</u>	<u>Gross amount offset on statement of financial condition</u>	<u>Net amounts on the statement of financial condition</u>	<u>Non cash collateral not netted on statement of financial condition (1)</u>	<u>Net amount</u>
December 31, 2021:					
Assets:					
Securities purchased under agreement to resell	\$ 1,341,202,037	—	1,341,202,037	(1,341,202,037)	—
Total assets	<u>\$ 1,341,202,037</u>	<u>—</u>	<u>1,341,202,037</u>	<u>(1,341,202,037)</u>	<u>—</u>

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	<u>Gross amount recognized</u>	<u>Gross amount offset on statement of financial condition</u>	<u>Net amounts on the statement of financial condition</u>	<u>Non cash collateral not netted on statement of financial condition (1)</u>	<u>Net amount</u>
December 31, 2021:					
Liabilities:					
Securities sold under agreement to repurchase	\$ 293,480,880	—	293,480,880	(293,480,880)	—
Total liabilities	<u>\$ 293,480,880</u>	<u>—</u>	<u>293,480,880</u>	<u>(293,480,880)</u>	<u>—</u>

- (1) According to ASC 210-20-45, for any additional amount subject to a master netting agreement but not offset on the statement of financial condition, entities should describe the rights of offset associated with recognized assets and liabilities subject to an enforceable master netting arrangement, derivative clearing agreement and repurchase agreement. As of December 31, 2021, the Company had master netting agreements with counterparties for the amounts in the above table but does not offset these amounts within the statement of financial condition.

The following table presents the gross amount of liabilities associated with repurchase agreements by remaining contractual maturity as of December 31, 2021:

	<u>Open and overnight</u>	<u>Up to 30 days</u>	<u>31-90 days</u>	<u>Greater than 90 days</u>	<u>Total</u>
Securities sold under agreement to repurchase	\$ 293,480,880	—	—	—	293,480,880
Total	<u>\$ 293,480,880</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>293,480,880</u>

The following table presents the gross amount of liabilities associated with repurchase agreement by class of underlying collateral as of December 31, 2021:

	<u>Repurchase agreement</u>
U.S. government securities	\$ 273,158,081
Foreign government securities	20,322,799
Total	<u>\$ 293,480,880</u>

The Company is required to post collateral with a market value equal to or in excess of the principal amount borrowed under repurchase agreements. To ensure that the market value of the underlying collateral remains sufficient, collateral is generally valued daily and the Company may be required to deposit additional collateral or may receive or return collateral pledged, when appropriate. Repurchase agreements are generally either overnight or short term. The Company manages liquidity risks related to these agreements by sourcing funding from a diverse group of counterparties, providing

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a range of securities collateral and pursuing longer durations, when appropriate. As of December 31, 2021, the Company had no repurchase to maturity transactions.

Refer to notes 2(g), 7(c) and 8(d) for further information on securities purchased under agreements to resell and securities sold under agreements to repurchase.

(5) Leveraged Leases

The Company entered into leveraged lease transactions, which are collateralized by security interests in the underlying assets. The components of leveraged leases at December 31, 2021 are detailed below, and receivable amounts are shown net of nonrecourse debt:

Receivables	\$	83,908,317
Unearned income		<u>(1,517,694)</u>
Total	\$	<u><u>82,390,623</u></u>

At December 31, 2021, total cash flows from leveraged lease receivables are due in the following contractual installments:

		<u>Receivables</u>
2022	\$	42,788,404
2023		—
2024		—
2025		—
Thereafter		<u>41,119,913</u>
Total	\$	<u><u>83,908,317</u></u>

As of December 31, 2021, leveraged leases totaled \$82,390,623 with related deferred tax liabilities of \$18,778,332. The Company is indemnified against credit and residual losses by SMBC Leasing and Finance, Inc. (“SMBC LF”) through a guarantee agreement. SMBC LF is also a subsidiary of the Parent. SMBC LF has adequate resources to perform under any such obligations that are reasonably expected to arise, and as such, the Company does not record an allowance for lease losses.

(6) Income Taxes

As of December 31, 2021, the Company’s deferred tax assets (DTA) and deferred tax liabilities (DTL) are as follows:

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Deferred tax assets:	
Employee bonus accrual	\$ 5,757,544
Investment in limited partnerships	4,170,668
Other	2,599,153
NOL for foreign branches	11,731,000
Less:	
Valuation allowance	<u>(11,731,000)</u>
Total deferred tax assets	<u>\$ 12,527,365</u>
Deferred tax liabilities:	
Book versus tax depreciation differences	2,782,797
Leveraged leases	<u>18,778,332</u>
Total deferred tax liabilities	<u>\$ 21,561,129</u>
Total deferred tax liabilities, net	<u><u>\$ 9,033,764</u></u>

The Company's deferred tax liabilities as of December 31, 2021 relate primarily to differences, between financial reporting and income tax purposes, in the timing of the recognition of income from the Company's investments in leveraged lease transactions, which are being accounted for as operating leases for tax purposes and as financing leases for financial statements purposes. Also, part of the deferred tax asset balances is \$11,731,000 for the UK Permanent Establishment (PE) unused net operation loss (NOLs). The Company recorded a valuation allowance against this asset because the Company believes that it is not more likely than not that the benefit from the NOL will be realized. Although the sixth advance pricing agreement (APA) covering the years from 2015 to 2019 determined that the Company does not have a PE in UK, the Company will continue to show this deferred asset since the UK NOL can be carried indefinitely.

As of December 31, 2021, the Company accrued \$2,508,084 of interest related to tax benefits. On a net of tax basis, the Company has accrued \$1,931,224 of interest as of December 31, 2021.

The Company is in the process of negotiating the seventh bilateral APA with the United States Internal Revenue Service (IRS) and United Kingdom HM Revenue and Customs which will govern the taxation of its activities in certain derivative financial instruments for tax years ended December 31, 2021 to December 31, 2024. The most recently signed APA methodology pertaining to tax years 2015 to 2019 is applied as a basis to estimate the impact of the pending APA.

It is the Company's policy that, pursuant to ASC 740, any state or local tax computed based on capital is considered to be a franchise tax.

Years after 2016 are open to Federal tax examination. All years subsequent to and including 2011 remain open to state and local tax examinations, including New York and California. The Company is currently under California, New York, and New York City examinations.

On February 6, 2019, the Company entered into Federal and state Tax Sharing Agreements with the Parent and each direct subsidiary of the Parent (members of the consolidated group). The effective date of the Tax Sharing Agreements

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is January 1, 2018. Consolidated Federal and, where applicable, state income tax returns for the year ended December 31, 2021 will be filed by the Parent. The separate return method applies ASC Topic 740 to the stand-alone financial statements of each member of the consolidated group as if the group member were a separate taxpayer and a stand-alone entity. Calculations of current and deferred taxes consider all applicable income tax laws for the relevant tax jurisdiction. For states where consolidated tax returns are not required, each member of the consolidated group will continue to file separate tax returns and pay taxes directly to the relevant tax authorities.

ASC 740-10-30-27 acknowledges that, under the separate return method, the sum of the amounts reported by individual members of the group may not equal the consolidated amount due to situations such as intercompany transactions between the subsidiaries of the Parent. Thus, if the tax sharing agreement differs from the chosen method of tax allocation under 740-10-30-27, the difference between the amount paid or received under the tax sharing agreement and the expected settlement amount based on the tax allocation method at the subsidiary level is treated as a dividend paid, or additional (paid-in) capital contribution (i.e., recorded in Equity). No such differences occurred in 2021.

Refer to note 2(m) for further details on income taxes.

(7) Fair Value of Financial Instruments

The Company measures fair value in accordance with ASC 820 using the methodologies set out below for all assets and liabilities measured at fair value.

In general, when available, the Company uses quoted market prices to determine fair value and classifies such items within Level 1. In some cases, where a market price is not available, the Company will make use of acceptable practical expedients (such as matrix pricing) to calculate fair value, in which case the items are classified within Level 2. If quoted market prices are not available, fair value is based upon internally developed models that use current market-based or independently sourced market parameters such as interest rates, currency rates, option volatilities, etc. If quoted market prices are not available, the valuation model used generally depends on the specific asset or liability being valued. The determination of fair value considers various factors, including interest rate yield curves, time value and volatility factors, underlying options, and derivatives and price activity for equivalent synthetic instruments.

Counterparty credit risk adjustments are applied to financial instruments such as over-the-counter derivatives, where the base valuation uses market parameters based on the LIBOR interest rate curves. Not all counterparties have the same credit ratings as that implied by the relevant LIBOR curve, so it is necessary to take into account the actual credit rating of a counterparty in order to arrive at the estimated value of such an instrument. Furthermore, the counterparty credit risk adjustment takes into account the effect of credit risk mitigants such as pledged collateral and to what extent there is a legal right of offset with a counterparty.

Bilateral or own credit risk adjustments are applied to reflect the Company's own credit risk when valuing all liabilities measured at fair value, in accordance with the requirements of ASC 820. The methodology is consistent with that applied in generating counterparty credit risk adjustments but incorporates SMBC's own credit risk as observed in the credit default swap market. As with counterparty credit risk, own credit risk adjustments include the impact of credit risk mitigants.

The Company incorporates the impact of funding in its valuation estimates where there is evidence that a market participant in the principal market would incorporate it in a transfer of the instrument. Funding adjustments are applied to reflect the expected funding cost integrated over the lifetime of the portfolio, with consideration of the default event

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of the counterparties. The Company's Funding Valuation Adjustment framework incorporates the impact of funding into its valuation estimates. The Company's approach for the funding adjustment includes assumptions related to the funding cost created by the mirror of any uncollateralized derivative assets.

Liquidity adjustments are applied to items in Levels 2 and 3 of the fair value hierarchy to ensure that the fair value reflects the price at which the entire position could be liquidated. The liquidity reserve is based on the bid/offer spread for an instrument.

The following tables present for each of the fair value hierarchy levels the Company's assets and liabilities that are measured at fair value on a recurring basis at December 31, 2021:

Assets at fair value as of December 31, 2021					
	Level 1	Level 2	Level 3	Netting agreements (a)	Total
Foreign exchange contracts	\$ —	4,487,581,448	24,345,777	—	4,511,927,225
Interest rate contracts	644,296,782	7,630,982,810	135,049	—	8,275,414,641
Other contracts	—	230,665	—	—	230,665
Subtotal	644,296,782	12,118,794,923	24,480,826	—	12,787,572,531
Cash collateral and counterparty netting	—	—	—	(10,750,028,440)	(10,750,028,440)
Derivative assets, net, at fair value	644,296,782	12,118,794,923	24,480,826	(10,750,028,440)	2,037,544,091
U.S. government securities	803,528,615	—	—	—	803,528,615
Foreign government securities	20,414,809	—	—	—	20,414,809
Other non-derivative	—	124,717,805	—	—	124,717,805
Trading assets, at fair value	823,943,424	124,717,805	—	—	948,661,229
Total	\$ 1,468,240,206	12,243,512,728	24,480,826	(10,750,028,440)	2,986,205,320

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Liabilities at fair value as of December 31, 2021					
	Level 1	Level 2	Level 3	Netting agreements (a)	Total
Foreign exchange contracts	\$ —	3,977,174,948	23,906,180	—	4,001,081,128
Interest rate contracts	132,436,227	6,808,134,014	2,806,647	—	6,943,376,888
Other contracts	—	1,493,370	—	—	1,493,370
Subtotal	132,436,227	10,786,802,332	26,712,827	—	10,945,951,386
Cash collateral and counterparty netting	—	—	—	(9,556,264,479)	(9,556,264,479)
Derivative liabilities, net, at fair value	132,436,227	10,786,802,332	26,712,827	(9,556,264,479)	1,389,686,907
U.S. government securities	698,932,727				698,932,727
Foreign government securities	69,540,197	—	—	—	69,540,197
Other non-derivative	—	1,006,680	—	—	1,006,680
Trading liabilities, at fair value	768,472,924	1,006,680	—	—	769,479,604
Total	\$ 900,909,151	10,787,809,012	26,712,827	(9,556,264,479)	2,159,166,511

(a) For contracts with the same counterparty, both cash collateral netting and counterparty nettings are included in the column titled “Netting agreements.” Refer to note 3 for further information on derivative financial instruments.

The following table provides quantitative information about significant unobservable inputs for Level 3 fair value measurements:

Level 3 assets at fair value as of December 31, 2021

Instrument	Fair value	Technique	Input	(W/Average)^(d)
Foreign exchange contracts	24,345,777	Model Based	(b)	(b)
Interest rate contracts	135,049	Model Based	(b)	(b) (c)

Level 3 liabilities at fair value as of December 31, 2021

Instrument	Fair value	Technique	Input	(W/Average)
Foreign exchange contracts	23,906,180	Model Based	(b)	(b)
Interest rate contracts	2,806,647	Model Based	(b)	(b)

(b) The derivative contracts categorized as level 3 consist of swaps whose fair value includes significant inputs to price the financial instrument in the form of uncertainties surrounding the full recognition of profits and model constraints or limitations that prohibit accurately pricing the transaction.

(c) The Company has an internal credit rating structure of 1-13, with 1 being the most creditworthy. The Company evaluates the creditworthiness of counterparties on a global basis and assigns internal credit ratings accordingly.

(d) Weighted averages are calculated based on the fair values of the instruments.

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Significant unobservable inputs for the derivative guarantees with a specific reserve are the internal credit ratings. A one notch increase (decrease) in the internal credit rating would result in a significantly lower (higher) fair value measurement of these financial instruments.

For derivative guarantees, the forward exposures used in the calculation of the credit valuation adjustment (CVA) are calculated using Monte Carlo simulations. The probability of default matrix is implied for market credit default swap (CDS) spreads. Refer to note 8(c) for further information on derivative guarantees.

The specific reserve for certain interest rate contracts was substantiated using the probability of default matrix implied from the spreads in a basket weighted CDS index in the marketplace. Therefore, these interest rate contracts will be classified within Level 2.

The following table provides a reconciliation of the beginning and ending balances for assets and liabilities measured at fair value using significant unobservable inputs (Level 3) for the year ended December 31, 2021.

	December 31, 2020	Transfers into Level 3	Transfers out Level 3	Purchases, issuances, and settlements	Net realized gains (losses)	Net unrealized gains (losses)	December 31, 2021
Assets							
Foreign exchange contracts	\$ —	24,345,777	—	—	—	—	24,345,777
Interest rate contracts	2,993,971	15,475	(1,954,344)	(505,262)	—	(414,791)	135,049
Total assets at fair value	<u>\$ 2,993,971</u>	<u>24,361,252</u>	<u>(1,954,344)</u>	<u>(505,262)</u>	<u>—</u>	<u>(414,791)</u>	<u>24,480,826</u>
Liabilities:							
Foreign exchange contracts	\$ 9,663,230	23,906,180	—	(9,663,230)	—	—	23,906,180
Interest Rate Contracts	—	2,806,647	—	—	—	—	2,806,647
Total liabilities at fair value	<u>\$ 9,663,230</u>	<u>26,712,827</u>	<u>—</u>	<u>(9,663,230)</u>	<u>—</u>	<u>—</u>	<u>26,712,827</u>

(a) Derivative Financial Instruments

Exchange traded derivative instruments are generally fair valued using quoted market (i.e., exchange) prices and so are classified within Level 1 of the fair value hierarchy.

The majority of derivative transactions entered into by the Company are executed over the counter and are valued using internal valuation techniques, as no quoted market prices exist for such instruments. The valuation technique and inputs depend on the type of derivative and the nature of the underlying. The principal techniques used to value these instruments are discounted cash flows, Black-Scholes, and Monte Carlo simulation.

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The key inputs depend upon the type of derivative and the nature of the underlying instrument and include interest rate yield curves, FX rates, and the spot price of the underlying, volatility, and correlation. A given position is categorized as Level 2 or Level 3 depending on the observability of the significant inputs to the model.

(b) *Trading Assets and Liabilities*

When available, the Company uses quoted market prices to determine the fair value of securities recorded within trading assets and liabilities; such items are classified in Level 1 of the fair value hierarchy.

Fixed income financial instruments included within trading assets and liabilities, and described in note 2(h), are valued using internal valuation techniques, as no quoted market prices exist for such instruments. The principal techniques used to value these instruments are discounted cash flows. The key inputs depend upon the type of instrument and the nature of the underlying and include interest rate yield curves, FX rates, and the spot price of the underlying. These fixed income instruments are categorized as Level 2.

Refer to notes 2(h) and 8(e) for further information on trading assets and liabilities.

(c) *Securities Purchased under Agreements to Resell and Securities Sold under Agreements to Repurchase*

Repos and reverse repos are not carried at fair value on the statement of financial condition, but are carried at amounts which approximate fair value due to their short term nature and negligible credit risk. The Company reports repos and reverse repos at contract prices, plus accrued interest.

Refer to notes 2(g), 4 and 8(d) for further information on securities purchased under agreements to resell and securities sold under agreements to repurchase.

(8) *Related-Party Transactions*

The Company has significant related-party balances with certain of its affiliates. The Company generally enters into these transactions in the ordinary course of business.

The following table sets forth related-party assets and liabilities as of December 31, 2021:

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Cash and cash equivalents	\$	364,029,809
Cash collateral pledged		241,380
Derivative assets, net, at fair value		149,923,099
Securities purchased under agreements to resell		911,997,717
Trading assets, at fair value		124,205,499
Investment in affiliate		200,000,000
Investment in limited partnerships		3,949,475
Other assets		<u>13,520,255</u>
Total assets	\$	<u><u>1,767,867,234</u></u>
Cash collateral received		161,399,307
Derivative liabilities, net, at fair value		1,025,728
Borrowings from affiliate		1,110,915,963
Other liabilities		<u>6,950,773</u>
Total liabilities	\$	<u><u>1,280,291,771</u></u>

(a) Cash and Cash Equivalents

At December 31, 2021, cash and cash equivalents held at SMBC was \$364,029,809, of which \$361,925,901 was on deposit with the SMBC Cayman Branch and earns interest at 0.07%. Accrued interest receivable at December 31, 2021 was \$704 (included in other assets).

Refer to note 2(d) for further information on cash and cash equivalents.

(b) Cash Collateral

The Company pledges and receives cash collateral based on the portfolio position. The affiliates have the right to request that the Company pledge collateral if the affiliates' current exposure to the Company exceeds a specified dollar value. The current exposure is calculated based on the market value of the derivative transactions with the affiliate. Transactions with the affiliates are subject to enforceable master netting agreements, and as such, all collateral has been presented net against the derivative positions.

(i) Cash Collateral Pledged

As of December 31, 2021, the Company pledged cash collateral, inclusive of accrued interest receivable and independent amounts, of \$40,320,240 of which, \$24,281,511 was to SMBC Nikko Securities Inc. ("SMBC Nikko Tokyo"), \$13,600,977 was to SMBC DP, \$2,337,752 was to SMBC Bank International PLC. ("SMBC BI"), and \$100,000 was to Manufacturers Bank ("MB"). Of these amounts, \$40,078,860 was offset against derivative liability positions, and \$241,380 was in excess of derivative liability positions and included in cash collateral pledged.

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(ii) *Cash Collateral Received*

As of December 31, 2021, the Company received cash collateral, inclusive of accrued interest payable of \$2,806,961,209, of which \$2,315,656,518 was from SMBC CM Ltd, \$266,156,863 was from SMBC, \$165,511,776 was from SMBC Aviation Capital related entities, \$29,402,510 was from SMBC Leasing (UK) Limited (“SMBC Leasing UK”), \$13,901,019 was from SMBC LF, \$8,580,618 was from MB, \$6,750,674 was from SMBC Leasing and Finance UK No. 1 Limited, \$700,048 was from CFT Investments 1 LLC (“CFT”), \$300,021 was from Mithras Leasing Ltd (“Mithras”), and \$1,162 was from other affiliates. Of these amounts, \$2,645,561,902 was offset against derivative asset positions, and \$161,399,307 was in excess of derivative asset positions and included in cash collateral received.

Refer to note 2(e) for further information on cash collateral pledged and received.

(c) *Derivatives, net, at fair value*

(i) *Derivative assets, net, at fair value*

At December 31, 2021 the Company had net derivative assets of \$149,923,099 of which \$144,989,032 with SMBC Aviation Capital related entities, \$1,186,290 was with SBF Funding, Inc. (“SBF”), \$1,075,662 was with CFT, \$903,635 was with SMBC Leasing UK, and \$1,768,480 with other affiliates.

(ii) *Derivative liabilities, net, fair value*

At December 31, 2021 the Company had net derivative liabilities of \$1,025,728 of which \$942,447 was with SMBC Nikko Tokyo and \$83,281 was with other affiliates.

(iii) *Guarantees*

The Company paid SMBC Tokyo Branch to provide a guarantee on Aviation Capital’s credit risk of certain derivative transactions as specified in agreements. Management concluded that these guarantee contracts meet the criteria of a credit derivative instrument as defined by ASC 815 and related guidance and are reported within derivative liabilities at fair value. Any credit reserves arising on such transactions are recognized by the Company and represent the fair market value of the derivative liabilities recorded within the statement of financial condition. For December 31, 2021 the Company recorded guarantees provided to Aviation Capital of \$165,284 at fair value within derivatives liabilities.

The Company has agreements with SMBC acting through SMBC Cayman Branch, which guarantee the prompt and complete payment when due of any net termination payment payable to the Company under any of the International Swaps and Derivatives Association Master Agreements of specific counterparties. A fee is payable monthly based on a rate ranging from 0.92% to 1.10% per annum of the monthly daily average value of the guarantee transactions. The guarantees qualify as derivative instruments under ASC 815, *Derivatives and Hedging*. Due to the related party relationship between SMBC and the Company and although the contract had a positive fair value from the Company’s perspective at inception, it was determined that the guarantee contracts should be treated as a capital transaction. As such, no net asset or capital contribution was recorded at the inception of the contract. The Company’s capital will be impacted as cash payments are made relative to the fee or claims under the guarantees are made by the Company and paid by SMBC. The guarantees meet the accounting definition of a guarantee under ASC 460, *Guarantees*.

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(d) *Securities Purchased under Agreements to Resell and Securities Sold under Agreements to Repurchase*

At December 31, 2021, the Company had securities purchased under agreements to resell of \$911,997,717 of which \$650,641,965 was with SMBC CM Ltd and \$261,355,752 was with SMBC Nikko SI.

Refer to notes 2(g), 4 and 7(c) for further information on securities purchased under agreements to resell and securities sold under agreements to repurchase.

(e) *Trading assets, at fair value*

Fixed income financial instruments and prepaid interest rate contracts, recorded within trading assets, and described in note 2(h), are outstanding with SMBC CM Ltd. and have a fair value of \$124,205,499 as of December 31, 2021.

Refer to notes 2(h) and 7(b) for further information on trading assets, at fair value.

(f) *Investment in Affiliate*

On December 28, 2007, SMBC CM Ltd. authorized the creation and issuance of 300,000,000 new, nonvoting, and perpetual noncumulative preference shares in six classes (Class A to Class F) with a notional value of \$1 each with a liquidation preference of \$1 each. The offered securities rank senior to the ordinary shares of SMBC CM Ltd. as to payment of dividends and in liquidation. 200,000,000 of these newly authorized preferred shares were allotted to and purchased by the Company at \$1 each. There is no obligation on the part of SMBC CM Ltd. to pay an annual dividend or interest on this class of share under any circumstances. The offered securities were redeemable on or after January 31, 2013 at the option of SMBC CM Ltd. As of December 31, 2021, there were no redemptions or dividends paid. Since the preferred shares do not have a readily determinable fair market value, they are within the scope of ASC Topic 321, *Investment-Equity Securities*. Impairment and income recognition guidance is not applicable to this investment.

(g) *Investment in Limited Partnership*

The Company has an investment in Moelis Group LP accounted for under the equity method of accounting. At December 31, 2021, the Company's investment balance was \$3,949,475.

Refer to note 2(n) for further information on the investment in limited partnership

(h) *Other Assets*

As of December 31, 2021, the Company had other assets of \$13,520,255 which consists of SLA fees, other receivables and reimbursable costs receivable.

(i) *SLA Fees*

The Company has service level agreements in place with related parties, in which the Company's employees act for the benefit of the related parties. The related parties agreed to reimburse proportionate share of the total compensation, benefits paid, and other expenses incurred to the Company for its services on the basis of service cost, or service cost plus a markup of either 7.5% or 10%. The Company has \$2,950,427 accrued fees, of which \$2,704,868 was with SMBC CM Ltd, and \$245,559 was with SMBC.

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(ii) *Reimbursable costs receivable*

The Company has reimbursable costs of \$10,535,718, of which \$6,048,668 was with SMBC CM Ltd, \$4,246,231 was with SMBC Nikko SI, \$219,424 was with SMBC, and \$21,395 was with the Parent and are included in other assets.

(iii) *Other Receivables*

The Company has other receivables of \$34,110, of which \$21,530 was with SMBC CM Ltd, \$11,876 was with SMBC Nikko SI, and \$704 was with SMBC Cayman Branch.

(i) ***Borrowings from Affiliate***

(i) *Committed Revolving Credit Facility*

On August 1, 2008, the Company entered into a committed revolving credit agreement with SMBC to allow the Company to draw funds for operating needs. The agreement was amended on January 31, 2014 to an amount of \$1,500,000,000 and has an interest rate of LIBOR plus 35 basis points. As of December 31, 2021, there were no amounts drawn under this facility. At December 31, 2021 the accrued commitment fee payable was \$381,250 (included in other liabilities).

(ii) *Uncommitted Revolving Credit Facility*

On June 30, 2006, the Company entered into an uncommitted revolving credit line agreement with SMBC in order to ensure that the Company has adequate funds to meet its short-term liquidity needs. This agreement was amended on January 31, 2017 to an amount of \$3,500,000,000. The borrowings issued under this facility as of December 31, 2021 had interest rates ranging from .130% to .565% and maturities ranging from 40 to 95 days. As of December 31, 2021, the Company has a loan outstanding from SMBC of \$1,110,915,963.

Refer to note 13 for further information on the uncommitted revolving credit facility.

(j) ***Other Liabilities***

As of December 31, 2021, the Company had other liabilities of \$6,950,773 which consists of accruals for various fees and reimbursable costs payable.

(i) *Credit Service Fees*

Credit service fees are paid related to certain derivative and related transactions. The Company utilizes the credit analysis conducted by SMBC in connection with entering into and monitoring certain derivative and related transactions. At December 31, 2021 the Company had credit service fees accrued of \$1,857,696 with SMBC.

(ii) *Other Payable*

At December 31, 2021 the Company had incurred costs payable to affiliates of \$3,941,636 of which \$3,454,585 was with SMBC, \$340,647 was with SMBC Nikko SI, and \$146,404 was with SMBC Americas Holdings Inc.

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(iii) *Agency Fees*

The Company engages SMBC CM Ltd. and SMBC CM Asia to execute trades in London and Hong Kong. In addition, SMBC CM Ltd. provides derivatives business services to the Company which includes marketing, operations, legal and systems services, while the Company provides the same derivative business services to SMBC CM Ltd. and further includes accounting, compliance, credit, risk analysis, management information reporting, project management and treasury services. Fees are either received or paid for the derivative business services provided pursuant to underlying agreements.

At December 31, 2021 the Company accrued agency fees payable of \$1,151,440 of which \$1,097,890 was payable to SMBC DP and \$53,550 was payable to SMBC CM Asia.

(9) Regulatory Capital

The Company is subject to regulatory capital requirements administered by CFTC. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's statement of financial condition. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company's assets, liabilities, certain off balance sheet items as calculated under regulatory accounting practices. The Company's capital amounts and classifications are subject to qualitative judgments by the regulators about components, risk weights, and other factors.

At December 31, 2021, the Company qualified as well capitalized under the regulatory framework for prompt corrective action as described under CFTC capital rules.

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum ratios of total, common equity Tier 1 capital (CET1), and Tier 1 capital to risk weighted assets (RWA). As of December 31, 2021, the Company met all capital adequacy requirements to which it is subject to.

The following is a reconciliation of stockholder's equity to CET1 as of December 31, 2021:

Stockholder's equity	\$ 1,725,297,316
Less:	
Intangible assets, net of associated DTL	3,950,717
Unrealized adjustments related to changes in fair value of liabilities	<u>15,405,341</u>
Total CET1	<u><u>\$ 1,705,941,258</u></u>

The Company's actual capital amounts and ratios computed in accordance with Company regulatory requirements are as follows:

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	Actual	Minimum Capital Requirement
CET1	\$ 1,705,941,258	\$ 20,000,000
CET1 to RWA ratio	1,705,941,258 (14.1%)	788,697,944 (6.5%)
Total capital to RWA ratio	1,705,941,258 (14.1%)	970,705,162 (8.0%)
Total capital to uncleared swap margin ratio	1,705,941,258 (21.5%)	633,724,952 (8.0%)

(10) Categories of Risk

(a) Market Risk

Market risk is the potential loss the Company may incur as a result of changes in the market value of a particular instrument. All financial instruments, including derivatives and short sales, are subject to market risk. The Company's exposure to market risk is determined by a number of factors, including the size, duration, composition, and diversification of positions held, the absolute and relative levels of interest rates and foreign currency exchange rates, as well as market volatility and illiquidity. For instruments such as options and warrants, the time period during which the options or warrants may be exercised and the relationship between the current market price of the underlying instrument and the option's or warrant's contractual strike or exercise price also affects the level of market risk. A significant factor influencing the overall level of market risk to which the Company is exposed is its use of hedging techniques to mitigate such risk. The Company manages market risk by setting risk limits and monitoring the effectiveness of its economic hedging policies and strategies.

In July 2017, the Financial Conduct Authority (the authority that regulates LIBOR) announced it intends to stop compelling banks to submit rates for the calculation of LIBOR after 2021. The Alternative Reference Rates Committee ("ARRC") has proposed that the Secured Overnight Financing Rate ("SOFR") is the rate that represents best practice as the alternative to USD-LIBOR for use in derivatives and other financial contracts that are currently indexed to USD-LIBOR. ARRC has proposed a paced market transition plan to SOFR from USD-LIBOR and currently the Company is implementing its transition plans as it relates to derivatives and cash markets exposed to USD-LIBOR.

Many of our existing assets and financial instruments do not include provisions clearly specifying a method for transitioning from LIBOR to an alternative benchmark rate, and it is not yet known how courts or regulators will view the transition away from LIBOR to an alternative benchmark rate. As a result, it is difficult to predict the impact that a cessation of LIBOR would have on the value and performance of our existing assets, liabilities or derivatives. The Company has a project underway to transition its LIBOR based contracts that have a maturity after 2021 and has started to execute some trades of SOFR based derivatives.

(b) Credit Risk

Credit risk is measured by the loss the Company would record if its counterparties failed to perform pursuant to the terms of their contractual obligations and the value of collateral held, if any, was not adequate to cover such losses. Specifically, the Company's potential credit loss exposure for contractual commitments is equal to the market or fair value of contractual commitments that are in a net asset position less the effect of enforceable master netting agreements. The Company has established controls to monitor the creditworthiness of counterparties, as well as the

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quality of pledged collateral, and uses master netting agreements whenever possible to mitigate the Company's exposure to counterparty credit risk. The Company may require counterparties to submit additional collateral when deemed necessary. The Company also enters into collateralized financing agreements in which it extends short term credit, primarily to major financial institutions. The Company controls the collateral pledged by the counterparties, which consists largely of securities issued by the U.S. government or its agencies.

The notional amounts of contractual commitments do not represent exposure to credit risk. Credit risk associated with futures contracts is limited since all transactions are guaranteed by the exchange on which they are traded and daily cash settlements by all counterparties are required for changes in the market value of open contracts. The Company's purchased exchange issued options also possess low credit risk due to guarantee of performance by the issuing exchange. Negotiated contractual commitments, such as forwards, swaps, and options possess greater exposure to credit risk since cash settlement is not normally required on a daily basis, and therefore, counterparty credit quality and the value of pledged collateral are essential elements in controlling the Company's risk.

Concentrations of credit risk from financial instruments, including contractual commitments, exist when groups of issuers or counterparties have similar business characteristics or are engaged in like activities that would cause their ability to meet their contractual commitments to be adversely affected, in a similar manner, by changes in the economy or other market conditions. The Company monitors credit risk on both an individual and group counterparty basis. The Company minimizes this risk through credit reviews, approvals, trading limits, and monitoring procedures.

(c) Model Risk

Model risk is the potential for adverse consequences from decisions based on incorrect or misused model outputs and reports. The Company's general perception regarding model risk includes any potential risk to the firm's operations, finances, or reputation arising out from errors or misuse of financial models. The Company manages model risk through effective governance and control of activities related to model development, model implementation and use, and model validation. Additionally, independence between model developers/users and those responsible for model validation is a critical element of effective challenge for the firm.

(d) Liquidity Risk

Liquidity risk is the risk that the Company will be unable to meet its contractual and contingent obligations or that it does not have the appropriate amount, composition and tenor of funding and liquidity to support its assets and liabilities.

The efficient management of liquidity is essential to the Company in retaining the confidence of the financial markets and ensuring that the business is sustainable. The Company manages liquidity risk through a control framework designed to maintain liquidity resources that are sufficient in amount and quality, and a funding profile that is appropriate for the firm. The control framework consists of policy formation, review and governance, analysis, stress testing, limit setting and monitoring.

(e) Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes or systems, human factors or due to external events.

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Operational risk is inherent in most aspects of our business, including the systems, processes and controls that support our activities. Operational risk can arise from human error, inappropriate conduct, failures in systems, processes and controls, or natural and man-made disasters. To manage operational risk, the Company has implemented an oversight and governance structure, within its operational risk framework, that focuses on the identification, assessment, reporting, monitoring, prevention and mitigation of operational risks, as well as timely and meaningful management reporting.

(11) Commitments

(a) Lease Commitments

The Company occupies office space under noncancelable operating subleases with SMBC, which the longest lease expires in 2037. In addition, the Company leases office space in accordance with the Company's Business Continuity and Disaster Recovery (BCDR) Plan. Future minimum rentals under the lease are estimated as follows:

		<u>Minimum rentals</u>
Year ending December 31:		
2022	\$	2,001,045
2023		1,868,802
2024		1,868,802
2025		1,868,802
2026		1,868,802
Thereafter		<u>18,157,281</u>
Total	\$	<u><u>27,633,534</u></u>

The Company shares BCDR office space with SMBC Nikko SI and expects repayment for certain costs in certain years.

(b) Committed Loan Facility

Under a loan agreement dated April 18, 2021, the Company has committed to provide SMBC DP with a \$200 million revolving credit facility for a five-year period. As of December 31, 2021, the entire facility was unused. A commitment fee on the amount of the undrawn facility is payable to the Company until the maturity date of the agreement.

(12) Employee Benefits Plans

The Company participates in the Sumitomo Mitsui Banking Corp. Retirement Plan, a noncontributory defined benefit retirement plan (the Retirement Plan), and in the Sumitomo Mitsui Banking Corp 401(k) Plan, a contributory defined contribution plan (the 401(k) Plan), sponsored by SMBC. The plans cover all salaried employees (with the exception of expatriates).

The Retirement Plan costs are allocated to the Company based on actuarial computations. No separate determination has been made of the actual present value of accumulated benefits and the Retirement Plan's assets as they relate to the employees of the Company. Participants in the 401(k) Plan may contribute up to \$19,500 (\$26,000 if age 50 or older) in

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2021, subject to certain limitations. The Company will match such 401(k) contributions in an amount equal to 100% of the first 3% of compensation, not to exceed the participants' contribution amount or 3% of the IRS compensation limit of \$290,000 for 2021.

(13) Subsequent Events

On January 31, 2022, the Company extended the maturity of its uncommitted revolving credit facility with SMBC to January 31, 2023. The amount on the uncommitted revolving credit facility remains unchanged at \$3,500,000,000. The facility allows the Company to draw funds for operating needs. Refer to note 8(i) for further detail on credit facilities.

The Company evaluated subsequent events through February 28, 2022, which is the date the statement of financial condition was available to be issued.