Company Registered Number: 25766

ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

REPORT OF THE DIRECTORS AND FINANCIAL STATEMENTS

31 December 2017

ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

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ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

BOARD OF DIRECTORS AND SECRETARY

DIRECTORS:	G Mallon (Executive Director) M Murphy (Independent Non-Executive Director) D O'Shea (Chairman and Independent Non-Executive Director) R Quinlan (Independent Non-Executive Director) P Stanley (Executive Director)
REGISTERED OFFICE:	Ulster Bank Group Centre George's Quay Dublin 2 D02 VR98
SECRETARY:	C Norris
AUDITORS:	Ernst & Young Chartered Accountants and Statutory Auditor Ernst & Young Building Harcourt Centre Harcourt Street Dublin 2 D02 YA40

ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

REPORT OF THE DIRECTORS

Presentation of information

In the Report and financial statements, and unless specified otherwise, the term 'the Bank' or 'UBIDAC' means Ulster Bank Ireland Designated Activity Company, 'the Group' or 'UBIDAC Group' means the Bank and its subsidiaries, 'NatWest Holdings' means NatWest Holdings Limited, 'RBS plc' means The Royal Bank of Scotland plc, 'RBSG' or 'the ultimate holding company' means The Royal Bank of Scotland Group plc and 'RBS Group' means the ultimate holding company and its subsidiaries.

The directors of UBIDAC present their report, together with audited financial statements of the Group for the financial year ended 31 December 2017. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union (EU).

Principal activities

The Bank, operating under the Ulster Bank brand, provides a comprehensive range of financial services through its Retail and Commercial Banking divisions. Retail Banking provides loan and deposit products through the Group's network of branches and direct channels, including the internet, mobile and telephony. Commercial Banking provides services to business and corporate customers, including small and medium enterprises. The Bank is regulated by the Central Bank of Ireland (CBI)/Single Supervisory Mechanism.

Business review

In December 2015, the CBI announced that it had written to a number of lenders requiring them to put in place a robust plan and framework to review the treatment of customers who have been sold mortgages with a tracker interest rate or with a tracker interest rate entitlement. The CBI stated that the intended purpose of the review was to identify any cases where customers' contractual rights under the terms of their mortgage agreements were not fully honoured, or where lenders did not fully comply with various regulatory requirements and standards regarding disclosure and transparency for customers. During the financial year the Group progressed its tracker mortgage examination programme. By 31 December 2017 1,038 customers had received remediation and compensation and the remainder are being contacted and remediated as quickly as possible. A charge of €87m has been recognised in 2017 based on an updated assessment of remediation and project costs, bringing the total amount provided since commencement of the review to €298m.

As part of an internal review of the wider retail and commercial loan portfolios, extending from the tracker mortgage examination programme, the Group identified further legacy business issues. A programme is ongoing to identify and remediate impacted customers and a charge of €100m has been recognised in 2017 based on expected remediation and project costs in relation to these items. Any issues relating to tracker mortgage products are included in the tracker mortgage examination provision as outlined above.

The directors continue to review how best to deleverage the Bank's balance sheet and specifically its strategy for addressing non-performing loans. During Q4 2017 the Board determined that it would seek to dispose of a further portfolio of non-performing loans during 2018 with a goal of delivering on the European Central Bank (ECB) requirements for banks to reduce their NPL ratios. Realising these assets over a shorter timeframe would reduce the value that the Group can expect to recover and therefore additional impairments have been recognised on these assets in December 2017.

The Bank's core ambition is to become the number one for customer service, trust and advocacy in its market by 2020. The directors are committed as a priority to resolving all outstanding remediation programmes relating to legacy issues. Other areas of focus for the Group in 2017 in working towards this ambition included growing new lending, supporting existing customers and digital innovation and development.

Through the 'Help for what matters' initiative the Bank continued to play an active role in supporting new and existing personal and business customers across the Republic of Ireland in achieving their ambitions.

In Retail Banking the 'Help for the movers' campaign contributed to new mortgage lending of €1bn in the financial year, matching that achieved in 2016. Lending continued to be driven by a strong uptake of both the Group's fixed and variable rate propositions supported by a team of mobile mortgage managers and through the mortgage broker channel where c.22% of new business was generated.

The Group continued to focus on strengthening its digital proposition, in particular enhancing and optimising its mobile capabilities. During 2017, 64% of the Group's customer base were 'digitally active', which included a 20% increase in mobile app users. A number of new features were introduced to the app, including the ability to make international payments and manage multiple business accounts through one login. 2017 also saw the introduction of both Apple Pay and Android Pay, meaning customers can now add their debit and credit cards to appropriately enabled devices to make contactless payments. Customers with the iPhone X are able to log into the app using the Face-ID function and all customers can utilise the 'Message us' function to chat to an adviser on a 24/7 basis.

Business review (continued)

The innovative ‘Get Cash’ feature that enables customers to withdraw cash from any Ulster Bank ATM without the use of their bank card was used over 83,000 times in 2017. The number of the Group’s customers opting for online statements via Anytime Banking has risen to 60%.

The significant developments in the Group’s digital proposition reflect ongoing trends in customer behaviour resulting in a reduction in usage of the traditional branch network. As a result the Group announced the closure of 22 branches. Simultaneously a programme of investment to upgrade the Group’s flagship branches was initiated, including enhanced data networks, the installation of automated service machines and the provision of in-branch Wi-Fi to offer customers a more comprehensive service. Significant developments in the Group’s digital proposition were complemented by the introduction of a team of Community Bankers. The Community Bankers engage with and support customers to understand the alternative options available to help them to meet their banking needs, including through digital channels and via An Post outlets. The Group also expanded its fleet of Mobile Banks or “banks on wheels” to five, with three new vehicles added in 2017. The fleet is operational five days per week serving customers across the Republic of Ireland.

Commercial Banking continued to support existing and new customers with credit provision resulting in a 10% increase in new lending to €1.39bn in 2017 from €1.26bn in 2016. New lending activity was particularly strong in the Corporate and Commercial Real Estate businesses where the Group is supporting growth in the market with the provision of finance across a number of sectors including healthcare, renewable energy, leisure and investment property within the Group’s risk appetite.

The Lombard Asset Financing business continued to build its SME and Corporate customer base, as well as further enhancing its consumer car finance offerings through the launch of Lombard Motor Finance, complementing its existing provision of stocking finance to vehicle dealers. In January 2017 the Group announced an expansion of its partnership with the Strategic Banking Corporation of Ireland to provide further lower-cost, flexible funding to independent SMEs and agri-businesses. Through the fund, developed in conjunction with the Department of Agriculture, Food and the Marine, the Bank offered €25m of working capital finance to the Agri sector throughout the Republic of Ireland.

In June 2017 the Group launched the Business Achievers network, an enhanced version of its previous ‘Small Business Can’ hub. This free, peer-to-peer digital platform currently has 20,000 registered business owners throughout Ireland. Users have the opportunity to share insights, generate collaboration and attract investment. The platform includes tools for messaging and networking, as well as event management and business planning, all of which are mobile enabled. The Group also hosted a series of seven supply chain events in conjunction with the Irish Exporters Association. The initiative brought together exporters and manufacturers from across the Republic of Ireland to discuss current challenges and opportunities and how the Group can best provide support whether through managing foreign exchange risk or aiding expansion to capitalise on market developments.

The Group also maintained its focus on innovation and investment in the development of its financial technology during 2017. The partnership with Dogpatch Labs, a leading co-working space for technology startups, entered its third year with the Group facilitating a third annual Hackathon, bringing together members of the external technology community to design, code and pitch ideas on banking innovations throughout the weekend-long event. A pilot project was established by the Group, in collaboration with a number of local financial institutions and consultancy firms, to explore newly developed blockchain technology. The initiative seeks to understand how the technology, developed by RBS in the UK, could improve the speed, resilience and security of domestic payment systems.

In 2017 the Group launched the Republic of Ireland’s first open banking Application Programme Interface. This technology is being developed in response to the EU’s Second Payment Services Directive and seeks to deliver greater control to customers over their finances, allowing them to choose more relevant and tailored financial services.

On 1 January 2017, as part of the response of RBS Group to the UK ring-fencing legislation to separate core banking activities and services from higher risk activities, NatWest Holdings, the holding company for the ring-fenced bank entities within RBS Group, acquired Ulster Bank (Ireland) Holdings Unlimited Company and its subsidiaries, including the Group, from Ulster Bank Limited. The Group and Bank are therefore positioned within the ring-fence with the Bank no longer a subsidiary of Ulster Bank Limited.

The directors continue to monitor the impact of the UK decision to leave the EU on the Group and its customers. There has been no material impact noted to date, however, the directors are conscious of the potential for future impacts on the Group, its operations, customers and staff. A Bank-wide Brexit response programme has been mobilised to assess those impacts and to develop contingencies under a number of Brexit scenarios to ensure that the Group can continue to provide its customers with a full range of services.

During the financial year the Group continued to support customers exploring expansion opportunities in the UK while also engaging with IDA Ireland and colleagues in RBS Group to help to identify businesses in the UK that are considering setting up operations in Ireland, with a view to providing banking products and services to them.

Business review (continued)

The Group continued with its strong corporate social responsibility ("CSR") agenda and holds the Business Working Responsibly Mark, the highest level of CSR accreditation in Ireland. The Group raised over €100k for its charity partners through its 'One Week In June' initiatives, including partnering with Irish Heart to raise funds for their FAST stroke awareness campaign. The Group entered its second year of partnership with Young Social Innovators, continuing to encourage staff to volunteer to support and mentor young people in their communities. MoneySense, the Bank's financial education programme for primary and secondary level students, has enjoyed continued success with multiple workshops held across the country, presented by volunteer staff from the Bank. The programme now also includes resources for parents and carers to use at home.

Financial performance

The Group's financial performance is presented in the Consolidated Income Statement on page 19.

The Group reported a total loss after tax for the financial year ended 31 December 2017 of €162m (2016: €37m profit) driven by a €206m movement in loan impairment provisions and a €39m decrease in income from trading activities offset by a €63m reduction in operating expenses.

Net interest income decreased by 4% to €471m. In 2017 there was a reduction on interest receivable on free funds, lower interest on impaired loans and increased interest payable on assets. This was partially offset by a reduction on interest payable on customer deposits due to repricing actions and lower interest payable on deposits by banks driven by rate movements.

Non-interest income decreased from €177m in 2016 to €138m, primarily due to reduced mark-to-market income on interest rate swaps and a €9m loss recognised on redemption of subordinated debt, partially offset by a decrease in fees payable on the Bank's committed funding facility with RBS.

Operating expenses decreased by 8% to €709m in 2017. Although the impact of charges in respect of legacy issues, including the tracker mortgage examination, was again significant in 2017 it reduced marginally year on year. The Group maintained a focus on reducing the underlying cost base, evidenced by reduced staff costs and a reduction in central cost charges from RBS Group. These were partially offset by an increase in provisions taken on the restructuring of the Group's property footprint.

The impairment loss of €68m represents a significant movement from the €138m gain in 2016. The 2016 gain was driven by improved residential and commercial property market conditions increasing collateral values and the release of provisions due to asset sales. Whilst residential and commercial property collateral values continued to increase in 2017 this was more than offset by the impacts of a change in non-performing loan strategy towards debt sale and refinements to the assumptions utilised in the Group's mortgage provisioning models.

The Group's capital position remained strong during 2017, as evidenced by the CET1 ratio of 31.2% at 31 December 2017 (2016: 29.8%). Total risk weighted assets (RWAs) reduced from €21.0bn in 2016 to €19.8bn at the balance sheet date.

At the financial year end the total assets of the Group were €30,248m (2016: €30,694m). Return on total assets for 2017 was -0.5% (2016: 0.1%).

Outlook

The directors note that economic data trends for the Republic of Ireland continue to be positive. The latest Central Statistics Office ('CSO') reports show annual economic (real GDP) growth of 7.4% in the first three quarters of 2017. The rate of unemployment fell for the twenty-first consecutive quarter to 6.9% in Q3 2017 and the number of people in employment increased by 2.2% year on year to Q3 2017. Both the Economic and Social Research Institute and the European Commission have predicted continued robust economic growth that will reduce moderately from current levels.

The Group remains vulnerable to changes and uncertainty in the external economic and political environment, which remained heightened in the past year. Scenarios identified as having a potentially material negative impact on the Bank include: global financial market volatility linked to advanced economy interest rate increases or decreases; a continued period of low interest rates; the impact of Brexit; vulnerabilities in emerging market economies resulting in contagion in the local market; a Eurozone crisis and major geopolitical instability.

With the introduction of IFRS 9 impairments are expected to be more volatile and the directors remain mindful of potential downside risks, particularly from single name and sector driven events.

Business review (continued)

Outlook (continued)

The directors, noting the continued and forecast economic growth and cognisant of the macroeconomic and political risks, consider that the actions the Group is taking on its legacy issues and the continued focus on strength and sustainability, customer experience, simplifying the Bank, supporting growth and employee engagement will assist in the delivery of the Group's ambition to be number one for customer service, trust and advocacy by 2020.

Risk management

The major risks associated with the Group's business are conduct and compliance, credit, market, liquidity and funding, reputational, operational, capital adequacy and business risk. The Group has a risk appetite framework for managing these risks and this is under continual evolution as the Group's business activities change in response to consumer market, credit, product, regulatory and other developments. The Group is also exposed to risks from its defined benefit pension schemes. The Group's policies for managing each of these risks and its exposure thereto are detailed in Note 24 to the financial statements.

A strong risk culture, underpinned by our values, is essential to the delivery of the ambition to build a truly customer-focused bank. To embed and strengthen risk culture in the Group a number of activities were undertaken in 2017. These included a "Risk Culture Week" sponsored by the Board and senior management, ethical scenario training, Group Policy Learning, and Managing Our Performance meetings designed to enhance risk culture at a team and individual employee level.

The Group's target risk culture behaviours have been embedded into Our Standards. These are clearly aligned to the core values of 'serving customers', 'working together', 'doing the right thing' and 'thinking long term'. They act as a clear starting point for a strong and effective risk culture because Our Standards are used for recruitment, selection and development of employees and performance management.

Accounting policies

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Details of the Group's critical accounting policies and key sources of estimation uncertainty are included in the accounting policies on pages 32 to 34.

Share capital presented as equity

Details of share capital presented as equity can be found in Note 21 to the financial statements.

Board of directors

The Board is the main decision-making forum for the Bank. It has overall responsibility for management of the business and affairs of the Group, the establishment of the Group strategy and the allocation and raising of capital, and is accountable to shareholders for financial and operational performance. The Board considers strategic issues and ensures the Group manages risk effectively through approving and monitoring the Group's risk appetite, considering Group stress scenarios and agreed mitigants and identifying longer term strategic threats to the Group's business operations. The Board's terms of reference includes key aspects of the Bank's affairs reserved for the Board's decision and are reviewed at least annually.

There are a number of areas where the Board has delegated specific authority to management, including the Chief Executive and Chief Financial Officer. These include responsibility for the operational management of the Group's businesses as well as reviewing high level strategic issues and considering risk appetite, risk policies and risk management strategies in advance of these being considered by the Board and/or its Committees.

Specific delegated authorities are also in place in relation to business commitments across the Group.

The roles of Chairman and Chief Executive are distinct and separate, with a clear division of responsibilities. The Chairman leads the Board and ensures the effective engagement and contribution of all executive and independent non-executive directors. The Chief Executive has responsibility for all Group businesses and acts in accordance with authority delegated by the Board. The independent non-executive directors combine broad business and commercial experience with independent and objective judgement and they provide independent challenge to the executive directors and leadership team.

Board and Executive Committees with delegation from the Board include:

The Group Audit Committee comprises two independent non-executive directors and assists the Board in discharging its responsibilities for the disclosure of the financial affairs of the Group. It reviews the accounting policies, financial reporting and regulatory compliance practices of the Group, the Group's systems and standards of internal controls, and monitors the Group's processes for internal audit and external audit.

Board of directors (continued)

The Board Risk Committee comprises two independent non-executive directors. It provides oversight and advice to the Board on current and potential future risk exposures of the Group and risk strategy. It reviews the Group's performance on risk appetite and oversees the operation of the Group Policy Framework.

The Nominations and Governance Committee comprises two independent non-executive directors and is chaired by the Chairman of the Group. It assists the Board in the selection and appointment of directors and senior management. It reviews the structure, size and composition of the Board, and membership and chairmanship of Board committees.

The Performance and Remuneration Committee comprises the three independent non-executive directors and advises the Board on remuneration matters.

The Related Party Lending Committee comprises of at least three members, two of whom are non-executive directors. The committee is responsible for approving lending to related parties, which are regulated under the CBI Code of Practice on Related Party Lending 2013.

The Board may from time to time seek to establish ad hoc sub committees to address key areas of focus. During 2017, two such committees were established – a Tracker and Mortgage Remediation Sub Committee, to focus on policy and remediation, and a Board Oversight Committee, established to oversee required enhancements to the governance and risk management practices in the Group. Both committees comprise of a mix of executive and independent non-executive directors.

The Executive Committee comprises the Group's senior executives and supports the Chief Executive in managing the Group's businesses. It reviews strategic issues and initiatives, monitors financial performance and capital allocations.

The Executive Risk Committee comprises the Group's senior executives, the directors and function heads of Risk and Compliance, and supports the Chief Executive in managing the Group's risk strategy, policy and risk management matters across the Group. The committee has delegated authority from the Executive Committee and reports to the Board Risk Committee.

Directors and secretaries

The directors and secretaries who served at any time during the financial year and up to the date of signing were as follows:

Directors	**Appointed**	**Resigned**
G Mallon		
M Murphy		
P Nolan		19 July 2017
D O'Shea		
R Quinlan		
P Stanley		
Secretaries		
S Anderson		14 September 2017
C Norris	14 September 2017	

In accordance with the Constitution, the directors are not required to retire by rotation.

Interests in shares or debentures

At 1 January and 31 December 2017, the directors and secretary did not have any interests in the shares or debentures of The Royal Bank of Scotland Group plc representing more than 1% of the nominal value of its issued share capital.

Employees

Staff engagement

The Group values the input of its employees and actively seeks opportunities to engage with all staff and invites them to contribute to on-going dialogue and activities to make the Bank a better bank for our customers and staff. The annual survey of employee opinions, known as 'Our View', provides valuable data to decision makers across the Group in support of improving employee engagement and satisfaction. We track our progress through pulse surveys during the financial year, utilising questions common across the financial services industry to compare ourselves against our peers. In addition we run an annual 'Working Together' survey where a representative sample provides feedback on the services provided by our support functions.

Employees (continued)

Staff engagement (continued)

Our community programmes focus on delivering genuine benefits that make a difference to people's lives throughout Ireland. The Group invests in programmes promoting financial education. Our employees across the Group continue to widely support, financially and through volunteering, many community and other worthy causes. Such activity is encouraged by the Group through its use of payroll giving and staff charity funds which support worthy causes at local, national and international level. Whilst our community programme ("Do Good, Feel Good") and activities run throughout the year, every June we have a particular focus and staff come together to raise funds for local and national charities. This programme offers staff a day to give their time as volunteers and fundraisers to a charity or cause that matters to them.

The Group promotes flexible working for all employees. We support staff to facilitate flexible working. Staff are able to avail of a range of flexible working options including regular or occasional working from home, working variable hours or working part time.

The Group is represented on the European Employee Council which facilitates dialogue amongst employee representatives in the European Economic Area.

Employment of people with disabilities

The Group's policy is that people with disabilities are always considered for employment and subsequent training, career development and promotion based on merit. If employees become disabled, it is the Group's policy, wherever possible, to retain them in their existing jobs or to re-deploy them in suitable alternative duties.

Diversity and inclusion

The Group has a Diversity and Inclusion Policy and values and promotes diversity in all areas of recruitment and employment. Building a working environment where all our staff can develop to their full potential is important to us irrespective of their age, belief, disability, ethnic or national origin, gender, gender identity, marital or civil partnership status, political opinion, race, religion or sexual orientation. We work to avoid limiting potential through bias, prejudice or discrimination. The Group recognises the beneficial contribution of a diverse mix of uniquely talented individuals for the delivery of great service to our diverse customer base. Key principles of our Diversity and Inclusion Policy include that we attract, motivate and retain the best talent. We base the employment relationship on the principles of fairness, respect and inclusion. We comply with local laws on equality and Our Code, which sets out the Group's expected behaviours and standards of conduct, to build and develop an inclusive workforce in order to understand and respond to our diverse customer base.

Safety, health and wellbeing

The Group recognises that people are key to the success of its business. The Group's vision is for its employees and communities to recognise that the Group's pride and performance in safety, health and wellbeing adds value to them and to the Group's business. Industry leading expertise, innovative tools, products and services and a practical approach to implementation are combined to ensure improved performance continues to be delivered.

Opportunities to improve the efficiency and effectiveness of safety, health and wellbeing policies and services were monitored and, where relevant, implemented. In 2017 we focused on improving wellbeing for our staff through the continued participation in the Virgin Pulse Challenge, with additional focus this year on mental health through the charity group, AWARE and participation in training in CPR through Irish Heart.

Policy and practice on payment of creditors

RBS Payables manages the creditors payments process on behalf of the Group. RBS Payables endeavours to pay the majority of suppliers of goods and services within one month of the Group receiving an appropriate invoice. In order to reduce administration costs certain smaller invoices may be held over for payment with larger invoices. Where a supplier requests it, RBS Payables will endeavour to accommodate specific payment terms. For the financial year the average trade creditor days period was 45 days (2016: 48 days).

Charitable contributions

During the financial year the Group made charitable and community investment donations in the Republic of Ireland totalling €316,976 (2016: €314,952).

Political donations

During the financial year the Group did not make any political donations (2016: €nil).

Branches outside the Republic of Ireland

The Bank and Group has a branch (as defined by Council Directive 89/666/EEC) in Northern Ireland.

Corporate Governance Code for Credit Institutions

The Corporate Governance Requirements for Credit Institutions 2015 ("the Code") imposes minimum core standards upon all credit institutions licensed or authorised by the CBI with additional requirements upon credit institutions which are designated as High Impact. The Bank has been designated as a High Impact credit institution and is therefore subject to the additional requirements for High Impact designation credit institutions included within Appendix 1 of the Code.

Corporate Governance Statement under Section 1373(2) of the Companies Act 2014

The Group operates internal control processes over financial reporting to support the preparation of the consolidated financial statements and manage risk in relation to financial statements preparation. The main components of this framework are as follows:

- a comprehensive set of accounting policies are in place to facilitate preparation of the annual financial statements in accordance with IFRS as adopted by the EU;
- a control process is in place involving the appropriate level of management review of significant account line items and disclosures to ensure that the financial information required for the financial statements is presented fairly and disclosed appropriately;
- the financial statements are subject to detailed review and approval by senior management and executive personnel within Finance and Risk with other specialists consulted as appropriate;
- a Disclosure Committee operates as a sub-committee of the Bank's Executive Committee to oversee, evaluate and review accounting issues and developments and recommendations on key accounting judgements including impairment provisions and valuations prior to presentation to the Bank's Audit Committee and Board;
- detailed papers are prepared for review and approval by the Bank's Audit Committee and Board setting out significant judgemental and technical accounting issues and any significant presentation and disclosure considerations;
- user access to financial reporting systems is restricted to those individuals that require it to fulfil their assigned roles and responsibilities; and
- Internal Audit, as the Bank's third Line of Defence, and in accordance with the Institute of Internal Auditors International Professional Practices Framework, provides independent assurance to the Board and executive management on the quality and effectiveness of governance, risk management and internal controls to monitor, manage and mitigate key risks to achieving the Bank's objectives.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position, including potential risks and uncertainties, are set out in the business review on pages 2 to 5.

The financial position of the Group, its cash flows, liquidity position, capital and funding sources are set out in the financial statements. Notes 9, 24 and 36 to the financial statements include the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to market, credit and liquidity risks.

The Group avails of a number of sources of liquidity including retail and commercial deposits, the European Central Bank's Targeted Long Term Refinancing Operation 2 ("TLTRO 2") and debt securities in issue. In March 2017 the Group entered into a €1bn uncommitted secured inter-group loan ("IGL") facility with RBS plc which remained fully undrawn in 2017. Furthermore, the Group's assets as at 31 December 2017 contain €2bn of short term liquidity instruments.

The Group's capital position remained strong during 2017, as evidenced by the CET1 ratio of 31.2% at 31 December 2017 (2016: 29.8%).

Having reviewed the Group's forecasts, projections and other relevant evidence, the directors have a reasonable expectation that the Group and the Bank will continue in operational existence for the foreseeable future. Accordingly, the financial statements of the Group and the Bank have been prepared on a going concern basis.

Accounting records

The measures taken by the directors to secure compliance with the requirements of Sections 281 to 285 of the Companies Act 2014 with regard to the keeping of accounting records are the employment of appropriately qualified accounting personnel and the maintenance of computerised accounting systems. The Company's accounting records are maintained at the Company's registered office at Ulster Bank Group Centre, George's Quay, Dublin 2, D02 VR98.

Investments in Group undertakings

Details of the Bank's investments in Group undertakings are shown in Notes 13 and 33. All of the Group undertakings are included in the Group's consolidated financial statements and all have an accounting reference date of 31 December.

Country-by-country reporting

The Bank has opted to publish the information required under Section 77 of Statutory Instrument S.I. No. 158 of 2014 requirements (country-by-country reporting) on its website: www.ulsterbank.ie.

Dividends

The Directors did not pay any interim dividends during the year (2016: €1,500m). The Directors do not recommend the payment of a final dividend (2016: €nil).

Post balance sheet events

In January 2018 the directors declared and paid an interim dividend of €1,500m.

Auditors

The auditors, Ernst & Young, Chartered Accountants and Statutory Audit Firm, will continue in office in accordance with the Companies Act 2014.

Directors' compliance statement

In accordance with the provisions of Section 225 of the Companies Act 2014, the directors acknowledge that they are responsible for securing the Bank's compliance with the relevant obligations, as defined by the Act. The directors confirm that:

- a compliance statement has been drawn up setting out the Group's policies in relation to complying with the relevant obligations;
- appropriate measures are in place that are designed to ensure material compliance with the relevant obligations; and
- the directors have carried out a review of these measures during the financial year.

Directors' disclosure to auditors

Each of the directors at the date of approval of this report confirms that:

(a) so far as the director is aware, there is no relevant audit information of which the Bank's auditors are unaware; and

(b) the director has taken all steps he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the Bank's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 330(1) of the Companies Act 2014.

On behalf of the Board:

Gerry Mallon
Chief Executive Officer

Des O'Shea
Chairman

16 February 2018

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the directors' report and the financial statements in accordance with the Companies Act 2014 and applicable regulations.

Irish company law requires the directors to prepare the financial statements for each financial year. Under company law, the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards as adopted by the European Union ("relevant financial reporting framework"). Under company law, the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the assets, liabilities and financial position of the Group and Bank as at the financial year end date and of the profit or loss of the Group and Bank for the financial year and otherwise comply with the Companies Act 2014.

In preparing these financial statements the directors are required to:

- select suitable accounting policies for the Bank and the Group financial statements and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether the financial statements have been prepared in accordance with applicable accounting standards, identify those standards, and note the effect and the reasons for any material departure from those standards; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Bank will continue in business.

The directors are responsible for ensuring that the Group and Bank keep or cause to be kept adequate accounting records which correctly explain and record the transactions of the Group and Bank, enable at any time the assets, liabilities, financial position and profit or loss of the Group and Bank to be determined with reasonable accuracy, enable them to ensure that the financial statements and directors' report comply with the Companies Act 2014 and enable the financial statements to be audited. They are also responsible for safeguarding the assets of the Group and Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities. The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Group's website.

By order of the Board:

Gerry Mallon Chief Executive Officer	Des O'Shea Chairman

16 February 2018

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

Opinion

We have audited the financial statements of Ulster Bank Ireland Designated Activity Company ('the Company') and its subsidiaries (all together, 'the Group') for the year ended 31 December 2017, which comprise the Consolidated Income Statement, Consolidated Statement of Comprehensive Income, the Group and Parent Company Balance Sheets, the Group and Parent Company Statements of Changes in Equity, the Group and Parent Company Cash Flow Statements and notes to the financial statements, including the summary of significant accounting policies set out in Note 1. The financial reporting framework that has been applied in their preparation is Irish Law and International Financial Reporting Standards ('IFRS') as adopted by the European Union and, as regards the Company financial statements, as applied in accordance with the provisions of the Companies Act 2014.

In our opinion:

- the Group financial statements give a true and fair view of the assets, liabilities and financial position of the group as at 31 December 2017 and of its loss for the year then ended;
- the Company financial statements give a true and fair view of the assets, liabilities and financial position of the company as at 31 December 2017;
- the Group financial statements have been properly prepared in accordance with IFRS as adopted by the European Union;
- the Company financial statements have been properly prepared in accordance with IFRS as adopted by the European Union as applied in accordance with the provisions of the Companies Act 2014; and
- the Group financial statements and Company financial statements have been properly prepared in accordance with the requirements of the Companies Act.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (Ireland) (ISAs (Ireland)) and applicable law. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Group and Company in accordance with ethical requirements that are relevant to our audit of financial statements in Ireland, including the Ethical Standard as applied to public interest entities issued by the Irish Auditing and Accounting Supervisory Authority (IAASA), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters, in relation to which ISAs (Ireland) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Group's and Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Overview of our audit approach

Key audit matters	• Impairment provision on loans and advances to customers • Conduct provisions • Recoverability of deferred tax assets • IT systems and controls • Valuation of derivative financial instruments with higher risk characteristics
Materiality	• Group materiality of €64m which represents 1% of Equity

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to the risk
Impairment provision on loans and advances to customers As at 31 December 2017, gross loans and advances to customers amounted to €23,214m (2016: €23,406m) and the related impairment provision amounted to €1,264m (2016: €1,392m). The basis of the impairment provision policy is presented in Note 1(z) 'Critical accounting policies and key sources of estimation uncertainty' and further analysed in Note 10 to the consolidated financial statements. The Group exercises significant judgement, using subjective assumptions, when determining both the timing and the amounts of the impairment provision for loans and advances. As retail and commercial loans and advances form a significant portion of the Group's assets, and due to the significance of judgement used in estimating both the specific and collective provisions, this is considered to be a key area of audit focus. We have focused on the following critical judgements and estimates which could give rise to material misstatement or are potentially subject to management bias: • The completeness and timing of recognition of loss events. • The measurement of individually assessed provisions, which is dependent on the valuation of collateral, the timing of cash flows and realisations. • The measurement of modelled provisions, which is dependent upon key assumptions relating to probability of default and recovery rates. Refer to the Accounting policies and Note 10 of the Consolidated Financial Statements	Impairment provisions recognised in respect of retail and commercial lending are determined by management using discounted cash flow assessments and modelling techniques that utilise customer data, historical loan performance, expected future performance and a variety of market assumptions. We focused on the assumptions underlying the calculation of modelled provisions and the discounted cash flow assessments. In obtaining sufficient audit evidence we: • Reviewed design and operating effectiveness of key controls around the end-to-end process of initiation, classification and performance monitoring, assessment and approval of impairment provisions, governance and model validation, with consideration given to susceptibility of controls to management override. • Tested key data inputs employed by modelling tools and impairment calculations. • Reviewed impairment methodology to establish model parameters and utilised our credit risk specialists to test the assumptions and calculations of modelled provisions. • For a risk based sample of loans, we performed file reviews to assess whether any IAS 39 loss indicators were present. • For non-performing loans, we tested a sample of the bank's loan reviews and assessed the measurement of the provisions and utilised our valuation specialists to value the collateral. We examined other cash flow assumptions where the level of provision is not dependent on collateral values. We also assessed the reasonableness of the timing of estimated cash flows. • Evaluated and challenged key assumptions adopted by management. • Assessed the appropriateness and presentation of disclosures with relevant accounting standards. Our planned audit procedures were completed without material exception.

Risk	Our response to the risk
Conduct provisions The continued heightened regulatory scrutiny gives rise to a high level of judgement in determining appropriate provisions and disclosures. At the year end the Group reported €467m (2016: €351m) of Provisions, accruals and other liabilities, of which €326m (2016: €201m) related to conduct provisions. Management judgement is needed to assess whether an obligation exists and a provision should be recorded at 31 December 2017 in accordance with the accounting criteria set under IAS 37. This includes determining if: • It is likely that an economic outflow such as a payment will occur; and • The amount of the payment (or other economic outflow) can be estimated reliably The measurement of the provision is based on the best estimate of the expenditure to settle the present obligation. The most significant areas of judgement are: • Completeness of provisions recognised; judgement in the determination of whether an outflow in respect of identified material conduct matters are probable or can be estimated reliably • Measurement of provisions recognised; Integrity and completeness of data, and the appropriateness of assumptions and judgements used in the estimation of material provisions • Adequacy of disclosures of contingent liabilities Refer to the Accounting policies and Notes 18 and 25 of the Consolidated Financial Statements	We tested the key controls over the identification, estimation and monitoring of provisions considering the potential for management override of controls. The controls tested include those implemented to assess the completeness and accuracy of data used to estimate provisions, and ensure the accuracy and completeness of disclosures made in accordance with accounting standards. In obtaining sufficient audit evidence we: • Assessed the provisions recorded by testing the data and assumptions used in the calculation of the provisions recorded. • We considered the policy decisions and the documentation supporting the Group's position including legal advice where available. • Reviewed the provision including programme costs to determine if the provision met the requirements of IAS 37. In addition, for matters where a provision was not recognised, we considered whether the outcome was probable and reliably estimable in accordance with the accounting criteria. • Where appropriate, we involved our conduct risk specialists. For key matters, we considered regulatory correspondence • We attended meetings with key management and reviewed the minutes of meetings of those charged with governance to conclude on the appropriateness of the conclusions reached. • We tested the disclosure provided on conduct provisions to determine whether it complied with accounting standards. Given the inherent estimation uncertainty and the judgemental nature of these provisions, we evaluated the appropriateness of the disclosure made in the financial statements. Our planned audit procedures were completed without material exception.

Risk	Our response to the risk
Recoverability of deferred tax assets	
The Group has deferred tax assets of €285m (2016: €293m), of which €292m (2016: €292m) arises from tax losses carried forward, reduced by €6m of pension related charges. As set out within Note 1(m) 'Accounting policies' and 1(z) 'Critical accounting policies and key sources of estimation uncertainty', the recognition and carrying value of deferred tax assets requires management judgement and estimation in assessing the probability and sufficiency of future taxable profits from which deductible temporary differences and unutilised tax losses can be offset. In light of the inherent uncertainty and significant amount of judgement and estimation required by management, we have considered future forecasts supporting the recognition of deferred tax assets to be an area of audit focus. Refer to the Accounting policies and Note 19 of the Consolidated Financial Statements	In the performance of our audit procedures, focus was placed on assessing the key judgement inputs and assumptions underlying the profit projections such as macro-economic assumptions, business growth rates, cost reduction and restructuring initiatives. In obtaining sufficient audit evidence we: • Tested the design and operating effectiveness of key controls around the preparation and review of budgets and forecasts supporting deferred tax assessment and profitability projections, including appropriate governance procedures and management challenge. • Reviewed and challenged inputs and assumptions embedded in forecasts, considering whether the overall forecasts are reasonable and achievable based on performance, our understanding of the business and the economic environment. • Assessed the reasonableness of deferred tax assets recognised in the context of the actual results, management profit projections and the Bank's strategic plans. • Evaluated how previous management forecasts compared to actual results to assess the accuracy of the forecasting process. Our planned audit procedures were completed without material exception.

Risk	Our response to the risk
IT systems and controls	
Our audit procedures have a focus on IT systems and controls due to the pervasive nature and complexity of the IT environment, the large volume of transactions processed in numerous locations daily and the reliance on automated and IT dependent manual controls. Key areas of audit focus included the changeover to a new General Ledger system during the year, user access management, developer access to the production environment and changes to the IT environment. The effectiveness of these areas is key to ensuring IT dependent and application based controls are operating effectively.	We tested the design and operating effectiveness of the Group's IT controls over the information systems that support critical business processes relevant to financial reporting. In obtaining sufficient audit evidence we: • Tested IT general controls (logical access, changes management and aspects of IT operational controls). This included testing that requests for access to systems were appropriately reviewed and authorised. • Tested the Group's periodic review of access rights. • Inspected requests of changes to systems for appropriate approval and authorisation and the assessment of segregation of duties between developers and those with the ability to promote changes to production. • Reviewed and assessed the control environment relating to various interfaces, configuration and other application layer controls identified as key to our audit. Our planned audit procedures were completed without material exception.

Risk	Our response to the risk
Valuation of derivative financial instruments with higher risk characteristics The Group's derivative products include swaps, forwards, futures and options. Valuation techniques used in assessing fair value vary and often involve a degree of estimation, the extent of which depends on the nature and complexity of each security. The valuation of complex level 3 derivative financial assets of €279m (2016: €429m) and complex level 3 derivative financial liabilities of €270m (2016: €575m) involves judgement and estimation giving rise to a risk of inappropriate balance sheet and revenue recognition. Refer to the Accounting policies and Note 9 of the Consolidated Financial Statements.	In light of the inherent difficulty associated with the valuation of complex derivative financial instruments, we focused our audit procedures on the assessment of fair value techniques adopted in deriving the year-end valuation. In obtaining sufficient audit evidence we: • Tested the design and operating effectiveness of the Group's controls over financial instrument valuations, governance and reporting. • Reviewed the appropriateness of the valuation models based on instrument types, considering any changes made to the models since prior year. • Revalued a sample of positions using EY modelling tools. • Verified and tested key inputs into valuation models, including data and key parameters. • Reviewed and challenged appropriateness of key assumptions used. • Assessed the appropriateness of valuation adjustments applied to the modelled price to capture the valuation uncertainty in line with IFRS 13. Our planned audit procedures were completed without material exception.

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

Materiality is the magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group to be €64m (2016: €65m), which equates to 1% of Equity (2016: 1%). We believe that Equity provides us with the most appropriate basis for materiality having considered the expectation of the users of the financial statements, the ultimate parent entity and the overall business environment.

Performance materiality

Performance materiality is the threshold for application of materiality at the individual account or balance level. Performance materiality is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the overall control environment, our judgement was that performance materiality should be set at 50% (2016: 50%) of our planning materiality, namely €32m (2016: €32m). We have set performance materiality at this percentage having considered our prior year experience of the risk of misstatements, both corrected and uncorrected.

Reporting threshold

The reporting threshold is set as the amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of €3.2m (2016: €3.2m), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. Our reporting threshold amount is designated at an amount below which misstatements would not be accumulated because we expect that the accumulation of such amounts clearly would not have a material effect on the financial statements.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

An overview of the scope of our audit report

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each entity within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the Group and effectiveness of Group wide controls, changes in the business environment and other factors such as recent Internal audit results when assessing the level of work to be performed at each entity.

There have been no significant changes in scoping from that applied in our prior year audit as all subsidiaries are included in full scope population and all audit work performed for the purposes of these financial statements was undertaken by the Group audit team.

Other information

The directors are responsible for the other information. Other information comprises the information included in the Annual Report other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2014

Based solely on the work undertaken in the course of the audit, we report that:

- in our opinion, the information given in the directors' report is consistent with the financial statements; and
- in our opinion, the directors' report has been prepared in accordance with the Companies Act 2014.

We have obtained all the information and explanations which we consider necessary for the purposes of our audit.

In our opinion the accounting records of the Company were sufficient to permit the financial statements to be readily and properly audited and the Company statement of financial position is in agreement with the accounting records.

Matters on which we are required to report by exception

Based on the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the directors' report.

The Companies Act 2014 requires us to report to you if, in our opinion, the disclosures of directors' remuneration and transactions required by sections 305 to 312 of the Act are not made. We have nothing to report in this regard.

Respective responsibilities

Responsibilities of directors for the financial statements

As explained more fully in the directors' responsibilities statement set out on page 10, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group and the Company's ability to continue as going concerns, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or the parent Company or to cease operations, or has no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (Ireland) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

The objectives of our audit, in respect to fraud, are; to identify and assess the risks of material misstatement of the financial statements due to fraud; to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and to respond appropriately to fraud or suspected fraud identified during the audit. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

Our approach was as follows:

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and have a direct impact on the preparation of the financial statements.
- We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur by holding discussions with senior management, including the Chief Financial Officer, Director of Risk, Head of Internal Audit and Group Audit Committee Chairman. We also reviewed the Group's fraud-related policies and mandates of different governance forums assessing fraud.
- As part of our audit procedures, we were aware of the risk of fraud, especially in the areas of estimation and those we assessed as having the risk of management override.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved inquiring of key management, reviewing the key policies and reviewing the correspondence exchanged with the Regulators.

A further description of our responsibilities for the audit of the financial statements is located on the IAASA's website at: http://www.iaasa.ie/getmedia/b2389013-1cf6-458b-9b8f-a98202dc9c3a/Description_of_auditors_responsibilities_for_audit.pdf.

This description forms part of our auditor's report.

Other matters which we are required to address

We were appointed by the board of Ulster Bank Ireland Designated Activity Company to audit the financial statements for the year ending 31 December 2016 and subsequent financial periods. The current period of total uninterrupted engagement including previous renewals and reappointments of the firm is 2 years.

The non-audit services prohibited by IAASA's Ethical Standard were not provided to the Group and we remain independent of the Group in conducting our audit.

Our audit opinion is consistent with the additional report to the audit committee.

The purpose of our audit work and to whom we owe our responsibilities

Our report is made solely to the Company's members, as a body, in accordance with section 391 of the Companies Act 2014. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Martina Keane
for and on behalf of
Ernst & Young Chartered Accountants and Statutory Audit Firm

Office: Dublin

Date: 22 February 2018

ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

CONSOLIDATED INCOME STATEMENT *for the financial year ended 31 December 2017*

		Group	
		2017	2016
	Note	**€m**	€m
Interest receivable		**545**	580
Interest payable		**(74)**	(91)
Net interest income	2	**471**	489
Fees and commission receivable		**114**	112
Fees and commission payable		**(9)**	(15)
Income from trading activities		**22**	61
Other operating income		**11**	19
Non-interest income	3	**138**	177
Total income		**609**	666
Operating expenses	4	**(709)**	(772)
Operating loss before impairment		**(100)**	(106)
Impairment (loss)/gain	10	**(68)**	138
Operating (loss)/profit before tax		**(168)**	32
Tax credit	7	**6**	5
(Loss)/profit for the financial year		**(162)**	37
Attributable to:			
Ordinary shareholders		**(162)**	37
		(162)	37

The accompanying notes form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME *for the financial year ended 31 December 2017*

	Group	
	2017	2016
	€m	€m
(Loss)/profit for the financial year	**(162)**	37
Items that will not be reclassified subsequently to profit or loss:		
Actuarial gains on defined benefit plans and other movements	**93**	113
Tax	**(12)**	-
Items that will be reclassified subsequently to profit or loss:		
Fair value (loss)/gains on available-for-sale financial assets	**(3)**	2
Other comprehensive income after tax	**78**	115
Total comprehensive (loss)/income for the financial year	**(84)**	152
Attributable to:		
Ordinary shareholders	**(84)**	152
	(84)	152

The accompanying notes form an integral part of these financial statements.

ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

BALANCE SHEETS *as at 31 December 2017*

		Group		Bank	
		2017	2016	**2017**	2016
	Note	**€m**	€m	**€m**	€m
Assets					
Cash and balances at central banks	9	**322**	290	**322**	290
Loans and advances to banks	9	**4,893**	4,622	**4,893**	4,303
Loans and advances to customers	9	**21,950**	22,014	**22,364**	22,499
Debt securities	11	**2,038**	2,340	**7,319**	10,071
Equity shares	12	**5**	6	**5**	6
Investments in Group undertakings	13	**-**	-	**5**	16
Derivatives	16	**582**	1,025	**554**	986
Intangible assets	14	**1**	-	**1**	-
Property, plant and equipment	15	**72**	78	**71**	77
Prepayments, accrued income and other assets	17	**35**	26	**34**	26
Retirement benefit assets	5	**62**	-	**62**	
Deferred taxation	19	**285**	293	**285**	293
Assets held for sale		**3**	-	**3**	-
Total assets		**30,248**	30,694	**35,918**	38,567
Liabilities					
Deposits by banks	9	**2,495**	1,675	**2,494**	1,674
Customer accounts	9	**19,817**	18,954	**25,522**	28,549
Debt securities in issue	9	**-**	1,377	**-**	-
Derivatives	16	**439**	886	**204**	351
Provisions, accruals and other liabilities	18	**467**	351	**465**	351
Retirement benefit liabilities	5	**11**	244	**11**	244
Subordinated liabilities	20	**616**	719	**616**	719
Total liabilities		**23,845**	24,206	**29,312**	31,888
Equity					
Non-controlling interests		**-**	1	**-**	-
Shareholders' equity:					
Called up share capital presented as equity	21	**3,592**	3,592	**3,592**	3,592
Reserves		**2,811**	2,895	**3,014**	3,087
Total equity		**6,403**	6,488	**6,606**	6,679
Total liabilities and equity		**30,248**	30,694	**35,918**	38,567

The accompanying notes form an integral part of these financial statements. As detailed in Note 8 the Bank's loss after tax for the year ended 31 December 2017 was €151m (2016: €380m profit).

The financial statements were approved by the Board of Directors on 16 February 2018 and signed on its behalf by:

Gerry Mallon	Des O'Shea	Paul Stanley	Caoimhe Norris
Chief Executive Officer	Chairman	Chief Financial Officer	Company Secretary

ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

STATEMENTS OF CHANGES IN EQUITY *for the financial year ended 31 December 2017*

	Group		Bank	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
Called up share capital presented as equity				
At 1 January and 31 December	**3,592**	3,592	**3,592**	3,592
Share premium account				
At 1 January and 31 December	**1,142**	1,142	**1,142**	1,142
Available-for-sale reserve				
At 1 January	**3**	1	**3**	1
(Loss)/gain in the financial year	**(3)**	2	**(3)**	2
At 31 December	**-**	3	**-**	3
Foreign exchange reserve				
At 1 January	**(2)**	23	**-**	-
Transfer to retained earnings	**2**	(25)	**-**	-
At 31 December	**-**	(2)	**-**	-
Retained earnings				
At 1 January	**1,752**	3,077	**1,942**	2,949
Actuarial gains on defined benefit plans and other movements	**93**	113	**93**	113
Tax	**(12)**	-	**(12)**	-
Transfer from foreign exchange reserve	**(2)**	25	**-**	-
(Loss)/profit attributable to ordinary shareholders	**(162)**	37	**(151)**	380
Dividends paid	**-**	(1,500)	**-**	(1,500)
At 31 December	**1,669**	1,752	**1,872**	1,942
Shareholders' equity at 31 December	**6,403**	6,487	**6,606**	6,679
Non-controlling interests				
At 1 January	**1**	1	**-**	-
Decrease in existing non controlling interests holdings	**(1)**	-	**-**	-
At 31 December	**-**	1	**-**	-
Total equity at 31 December	**6,403**	6,488	**6,606**	6,679

Total comprehensive (loss)/profit recognised in the statement of changes in equity is attributable as follows:

Ordinary shareholders	**(84)**	152	**(73)**	495
	(84)	152	**(73)**	495

The accompanying notes form an integral part of these financial statements.

ULSTER BANK IRELAND DESIGNATED ACTIVITY COMPANY

CASH FLOW STATEMENTS *for the financial year ended 31 December 2017*

		Group		Bank	
		2017	2016	**2017**	2016
	Note	**€m**	€m	**€m**	€m
Operating activities					
Operating (loss)/profit before tax		**(168)**	32	**(157)**	374
Adjustments for:					
Depreciation, amortisation and impairment of property, plant and equipment		**12**	10	**12**	10
Interest on subordinated liabilities		**5**	6	**5**	6
Dividends received		**-**	-	**(30)**	-
Charge for defined benefit pension schemes		**32**	43	**32**	43
Cash contribution to defined benefit pension schemes		**(234)**	(97)	**(234)**	(97)
Impairment loss/(gain) on loans and advances		**68**	(138)	**68**	(138)
Loan and advances written-off net of recoveries		**(128)**	(2,489)	**(128)**	(2,489)
Impairment of investments in Group undertakings		**-**	-	**2**	1
Elimination of foreign exchange differences		**(16)**	(71)	**(16)**	(69)
Other provisions charged net of releases		**200**	200	**200**	200
Other non-cash items		**125**	(270)	**124**	(271)
Net cash flows from trading activities	26	**(104)**	(2,774)	**(122)**	(2,430)
Changes in operating assets and liabilities		**1,882**	5,417	**809**	4,596
Net cash flows from operating activities before tax		**1,778**	2,643	**687**	2,166
Income taxes paid		**(3)**	(3)	**(2)**	(2)
Net cash flows from operating activities	26	**1,775**	2,640	**685**	2,164
Investing activities					
Sale and maturity of debt securities		**1,355**	1,830	**1,355**	1,830
Purchase of debt securities		**(1,124)**	(1,640)	**(1,124)**	(1,640)
Sale of equity shares		**(1)**	(1)	**(1)**	(1)
Sale of property, plant and equipment		**3**	15	**3**	4
Purchase of property, plant and equipment		**(12)**	(5)	**(12)**	(5)
Dividends received		**1**	2	**31**	2
Net cash flows from investing activities		**222**	201	**252**	190
Financing activities					
Redemption of debt securities in issue		**(1,377)**	(628)	**-**	-
Redemption of subordinated liabilities		**(100)**	-	**(100)**	-
Interest on subordinated liabilities		**(5)**	(6)	**(5)**	(6)
Repayment of non-controlling interest investment		**(1)**	-	**-**	-
Dividends paid		**-**	(1,500)	**-**	(1,500)
Net cash flows from financing activities		**(1,483)**	(2,134)	**(105)**	(1,506)
Effect of exchange rate changes on cash and cash equivalents		**(9)**	(4)	**(9)**	(4)
Net increase in cash and cash equivalents		**505**	703	**823**	844
Cash and cash equivalents 1 January	29	**4,966**	4,263	**4,648**	3,804
Cash and cash equivalents 31 December	29	**5,471**	4,966	**5,471**	4,648

The accompanying notes form an integral part of these financial statements.

1. Accounting policies

a) Presentation of financial statements

The consolidated financial statements are prepared on a going concern basis and in accordance with IFRS issued by the International Accounting Standards Board (IASB), and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB, as adopted by the EU. The Group and Bank's financial statements are presented in accordance with the Companies Act 2014 and the European Communities (Credit Institutions: Financial Statements) Regulations, 2015.

The Bank is incorporated and registered in the Republic of Ireland The Group and Bank's financial statements are prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: held-for-trading financial assets and financial liabilities, financial assets and financial liabilities that are designated as at fair value through profit or loss and available-for-sale financial assets. Recognised financial assets and financial liabilities in fair value hedges are adjusted for changes in fair value in respect of the risk that is hedged.

b) Basis of consolidation

The Bank controls another entity (a subsidiary) when it is exposed, or has rights, to variable returns from its involvement with that entity and has the ability to affect those returns through its power over the other entity; power generally arises from holding a majority of voting rights. The consolidated financial statements incorporate the financial statements of the Bank and entities (including certain special purpose entities) that are controlled by the Bank (its subsidiaries).

There are a number of entities in which the Bank holds less than half the voting rights which are consolidated when the substance of the relationship between the Bank and the entity indicates that the entity is controlled by the Bank.

On acquisition of a subsidiary, its identifiable assets and liabilities are included in the consolidated financial statements at their fair value. Any excess of the cost (the fair value of assets given, liabilities incurred or assumed and equity instruments issued by the Group plus any directly attributable costs) of an acquisition over the fair value of the net assets acquired is recognised as goodwill. The interest of non-controlling shareholders is stated at their share of the fair value of the subsidiary's net assets excluding shareholders loans.

A subsidiary is included in the consolidated financial statements from the date control transfers until the Group ceases to control them through a sale or significant change in circumstances. Changes in interest that do not result in a loss of control are recognised in equity. Total comprehensive income of subsidiaries is attributed to the owners of the Group and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

All intra-group balances, transactions, income and expenses are eliminated on consolidation. The consolidated financial statements are prepared using uniform accounting policies.

c) Assets held for sale

A non-current asset or a disposal group is classified as held for sale if the Group will recover its carrying amount principally through a sale transaction rather than through continuing use. A disposal group is a collection of assets and the liabilities directly associated with them that are intended to be transferred in a single transaction.

A non-current asset or disposal group classified as held for sale is measured at the lower of its carrying amount and fair value less costs to sell. If the asset or disposal group is acquired as part of a business combination it is initially measured at fair value less costs to sell. Assets and liabilities of disposal groups classified as held for sale and non-current assets classified as held for sale are shown separately on the face of the balance sheet.

d) Revenue recognition

Interest income and expense on financial assets that are classified as loans and receivables or available-for-sale and interest expense on financial liabilities other than those at fair value through profit or loss is determined using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or liabilities) and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. Calculation of the effective interest rate takes into account fees payable or receivable that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual terms of a financial instrument are considered when estimating future cash flows. Where negative effective interest rates apply to financial assets the related interest expense is shown as a separate item in interest payable.

Financial assets and financial liabilities held-for-trading or designated as at fair value through profit or loss are recorded at fair value. Changes in fair value are recognised through non-interest income together with dividends and interest receivable and payable.

1. Accounting policies (continued)

d) Revenue recognition (continued)

Fees in respect of services are recognised as the right to consideration accrues through the provision of the service to the customer. The arrangements are generally contractual and the cost of providing the service is incurred as the service is rendered. The price is usually fixed and always determinable. The application of this policy to significant fee types is outlined below.

Payment services: this income comprises income received for payment services including cheques cashed and direct debits. These are generally charged on a per transaction basis. The income is earned when the payment or transaction occurs. Charges for payment services are usually debited to the customer's account monthly or quarterly in arrears. Income is accrued at period end for services provided but not charged.

Card related services: fees from credit and debit card business include:

- Interchange received: as issuer, the Group receives a fee (interchange) each time a cardholder purchases goods and services. The Group also receives interchange fees from other card issuers for providing cash advances through its branch and automated teller machine networks. These fees are accrued once the transaction has taken place; and
- Periodic fees payable by credit card or debit card holders are deferred and taken to profit or loss over the period of the service.

Lending (credit facilities): commitment and utilisation fees are determined as a percentage of the outstanding facility. If it is unlikely that a specific lending arrangement will be entered into such fees are taken to profit or loss over the life of the facility otherwise they are deferred and included in the effective interest rate on the advance.

Brokerage fees: in respect of securities, foreign exchange, futures or options transactions entered into on behalf of a customer are recognised as income on execution of a significant act.

Trade finance: income from the provision of trade finance is recognised over the term of the finance unless specifically related to a significant act, causing income to be recognised when the act is executed.

Investment management fees: fees charged for managing investments are recognised as revenue as the services are provided. Incremental costs that are directly attributable to securing an investment management contract are deferred and charged as an expense as the related revenue is recognised.

Fees and commissions payable: fees and commissions are payable in respect of services provided by third party intermediaries. These are charged through profit or loss over the life of the underlying product.

e) Pensions and other post-retirement benefits

The Group provides post-retirement benefits in the form of pensions to eligible employees.

For defined benefit schemes, scheme liabilities are measured on an actuarial basis using the projected unit credit method and discounted at a rate that reflects the current rate of return on a high quality corporate bond of equivalent term and currency to the scheme liabilities. Scheme assets are measured at their fair value. Past service costs are recognised immediately to the extent that benefits have vested; otherwise they are amortised over the period until the benefits become vested. A defined benefit asset is limited to the present value of any economic benefits available to the Group in the form of refunds from the plan or reduced contributions to it.

Any surplus or deficit of scheme assets over liabilities adjusted for unrecognised actuarial gains and losses and past service costs is recognised on the balance sheet as an asset (surplus) or liability (deficit).

Contributions to defined contribution pension schemes are recognised in the income statement when payable.

f) Intangible assets

Intangible assets are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to profit or loss over the assets' estimated economic lives using methods that best reflect the pattern of economic benefits and is included in depreciation and amortisation. These estimated useful economic lives are between 3 and 12 years.

Direct costs relating to the development of internal-use computer software are capitalised once technical feasibility and economic viability have been established. These costs include payroll, the costs of materials and services, and directly attributable overheads. Capitalisation of costs ceases when the software is capable of operating as intended. During and after development, accumulated costs are reviewed for impairment against the benefits that the software is expected to generate. Costs incurred prior to the establishment of technical feasibility and economic viability are expensed as incurred, as are all training costs and general overheads. The costs of licences to use computer software that are expected to generate economic benefits beyond one year are also capitalised.

1. Accounting policies (continued)

g) Property, plant and equipment

Items of property, plant and equipment (except investment properties – see accounting policy i) are stated at cost less accumulated depreciation (see below) and accumulated impairment losses. Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for separately.

Depreciation is charged to profit or loss on a straight-line basis so as to write off the depreciable amount of property, plant and equipment (including assets owned and let on operating leases) over their estimated useful lives. The depreciable amount is the cost of an asset less its residual value. Freehold land is not depreciated. Estimated useful lives are as follows:

Freehold and long leasehold buildings	50 years
Short leaseholds	unexpired period of the lease
Property adaptation costs	10 to 15 years
Computer equipment	up to 5 years
Other equipment	4 to 15 years

The residual value and useful life of property, plant and equipment are reviewed at each balance sheet date with the effect of any changes in estimate accounted for on a prospective basis.

h) Impairment of non-financial assets

At each reporting date, the Group assesses whether there is any indication that the value of its non-financial assets is impaired. If any such indication exists, the Group estimates the recoverable amount of the asset and the impairment loss, if any. The recoverable amount of an asset is the higher of its fair value less cost to sell and its value in use. Value in use is the present value of future cash flows from the asset or cash-generating unit discounted at a rate that reflects market interest rates adjusted for risks specific to the asset or cash-generating unit that have not been reflected in the estimation of future cash flows. If the recoverable amount of a non-financial asset is less than its carrying value, an impairment loss is recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss. A reversal of an impairment loss on non-financial assets is recognised as it arises provided the increased carrying value does not exceed that which it would have been had no impairment loss been recognised.

i) Investment properties

Investment property, which is property held to earn rentals and/or for capital appreciation (including property under construction for such purposes), is measured initially at its cost, including transaction costs. Subsequent to initial recognition, investment property is measured at fair value. Fair value is based on current prices for similar properties in the same location and condition using internal valuation models based on yield comparables and any available recent market transactions taking cognisance of the principles of the Royal Institute of Chartered Surveyors (RICS) valuation methodology. Any gain or loss arising from a change in fair value is recognised in profit or loss.

Rental income from investment property is recognised on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income.

j) Foreign currencies

The Group's consolidated financial statements are presented in Euro, which is the functional currency of the Bank.

Group entities record transactions in foreign currencies in their functional currency - the currency of the primary economic environment in which they operate - at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the relevant functional currency at the foreign exchange rates ruling at the balance sheet date. Foreign exchange differences arising on the settlement of foreign currency transactions and from the translation of monetary assets and liabilities are reported in income from trading activities except for differences arising on cash flow hedges and hedges of net investments in foreign operations.

Non-monetary items denominated in foreign currencies that are stated at fair value are translated into the relevant functional currency at the foreign exchange rates ruling at the dates the values are determined. Translation differences arising on non-monetary items measured at fair value are recognised in profit or loss except for differences arising on available-for-sale non-monetary financial assets, for example equity shares, which are recognised in other comprehensive income unless the asset is the hedged item in a fair value hedge.

Assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into Euro at foreign exchange rates ruling at the balance sheet date. Income and expenses of foreign operations are translated into Euro at average exchange rates unless these do not approximate to the foreign exchange rates ruling at the dates of the transactions. Foreign exchange differences arising on the translation of a foreign operation are recognised in other comprehensive income. The amount accumulated in equity is reclassified from equity to profit or loss on disposal or partial disposal of a foreign operation.

1. Accounting policies (continued)

k) Leases

As lessor
Contracts with customers to lease assets are classified as finance leases if they transfer substantially all the risks and rewards of ownership of the asset to the customer. All other contracts with customers to lease assets are classified as operating leases.

Finance lease receivables are included in the balance sheet, within loans and advances to customers, at the amount of the net investment in the lease being the minimum lease payments and any unguaranteed residual value discounted at the interest rate implicit in the lease. Finance lease income is allocated to accounting periods so as to give a constant periodic rate of return before tax on the net investment and included in interest receivable. Unguaranteed residual values are subject to regular review to identify potential impairment. If there has been a reduction in the estimated unguaranteed residual value, the income allocation is revised and any reduction in respect of amounts accrued is recognised immediately.

Rental income from operating leases is credited to the income statement on a receivable basis over the term of the lease. Operating lease assets are included within property, plant and equipment and depreciated over their useful lives (see accounting policy g). Operating lease rentals receivable are included in other operating income.

As lessee
Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the relevant lease.

l) Provisions and contingent liabilities

The Group recognises a provision for a present obligation resulting from a past event when it is more likely than not that it will be required to transfer economic benefits to settle the obligation and the amount of the obligation can be estimated reliably.

If the Group has a contract that is onerous, it recognises the present obligation under the contract as a provision. An onerous contract is one where the unavoidable costs of meeting the obligations under it exceed the expected economic benefits. When the Group vacates a leasehold property, a provision is recognised for the costs under the lease less any expected economic benefits (such as rental income).

Contingent liabilities are possible obligations arising from past events whose existence will be confirmed only by uncertain future events or present obligations arising from past events that are not recognised because either an outflow of economic benefits is not probable or the amount of the obligation cannot be reliably measured. Contingent liabilities are not recognised but information about them is disclosed unless the possibility of any outflow of economic benefits in settlement is remote.

m) Taxation

Income tax expense or income, comprising current tax and deferred tax, is recorded in the income statement except income tax on items recognised outside profit or loss which is credited or charged to other comprehensive income or to equity as appropriate.

Current tax is income tax payable or recoverable in respect of the taxable profit or loss for the year arising in income or in equity. Provision is made for current tax at rates enacted or substantively enacted at the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable in respect of temporary differences between the carrying amount of an asset or liability for accounting purposes and its carrying amount for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that they will be recovered. Deferred tax is not recognised on temporary differences that arise from initial recognition of an asset or liability in a transaction (other than a business combination) that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax is calculated using tax rates expected to apply in the periods when the assets will be realised or the liabilities settled, based on tax rates and laws enacted, or substantively enacted, at the balance sheet date.

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to offset and where they relate to income taxes levied by the same taxation authority either on an individual Group company or on Group companies in the same tax group that intend, in future periods, to settle current tax liabilities and assets on a net basis or on a gross basis simultaneously.

1. Accounting policies (continued)

n) Financial assets

On initial recognition financial assets, as defined by IAS 39 'Financial Instruments: Recognition and Measurement', (IAS 39), are classified into: held-for-trading; designated as at fair value through profit or loss; loans and receivables; or available-for-sale. Regular way purchases of financial assets classified as loans and receivables are recognised on settlement date; all other regular way purchases are recognised on trade date.

Held-for-trading - a financial asset is classified as held-for-trading if it is acquired principally for sale in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative (not in a qualifying hedge relationship). Held-for-trading financial assets are recognised at fair value with transaction costs being recognised in profit or loss. Subsequently they are measured at fair value. Gains and losses on held-for-trading financial assets are recognised in profit or loss as they arise.

Designated as at fair value through profit or loss - financial assets may be designated as at fair value through profit or loss only if such designation: (a) eliminates or significantly reduces a measurement or recognition inconsistency; or (b) applies to a group of financial assets, financial liabilities or both, that the Group manages and evaluates on a fair value basis; or (c) relates to an instrument that contains an embedded derivative which is not evidently closely related to the host contract.

Financial assets that the Group designates on initial recognition as being at fair value through profit or loss are recognised at fair value, with transaction costs being recognised in profit or loss and are subsequently measured at fair value. Gains and losses on financial assets that are designated as at fair value through profit or loss are recognised in profit or loss as they arise.

Loans and receivables - non-derivative financial assets with fixed or determinable repayments that are not quoted in an active market are classified as loans and receivables, except those that are classified as available-for-sale or as held-for-trading, or designated as at fair value through profit or loss. Loans and receivables are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at amortised cost using the effective interest method (see accounting policy d) less any impairment losses.

Available-for-sale - financial assets that are not classified as held-to-maturity; held-for-trading; designated as at fair value through profit or loss; or loans and receivables are classified as available-for-sale. Financial assets can be designated as available-for-sale on initial recognition. Available-for-sale financial assets are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at fair value. Unquoted equity investments whose fair value cannot be measured reliably are carried at cost and classified as available-for-sale financial assets. Impairment losses and exchange differences resulting from retranslating the amortised cost of monetary available-for-sale financial assets denominated in a foreign currency are recognised in profit or loss together with interest calculated using the effective interest method (see accounting policy d). Other changes in the fair value of available-for-sale financial assets and any related tax are reported in a separate component of shareholders' equity until disposal, when the cumulative gain or loss is recognised in profit or loss.

Fair value – the Group's approach to determining the fair value of financial instruments is set out in the section of critical accounting policies and key sources of estimation uncertainty entitled Fair value - financial instruments; further details are given in Note 9.

o) Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or group of financial assets classified as available-for-sale or loans and receivables is impaired. Loans (including lendings under revolving facilities) with an impairment provision must be reported as an impaired loan. This includes loans granted forbearance where there is an economic loss and therefore an impairment provision.

Financial assets carried at amortised cost - if there is objective evidence that an impairment loss on loans and receivables has been incurred, the Group measures the amount of the loss as the difference between the carrying amount of the asset or group of assets and the present value of estimated future cash flows discounted at the original effective interest rate of the instrument at initial recognition. For collateralised loans and receivables, estimated future cash flows include cash flows that may result from foreclosure less the costs of obtaining and selling the collateral, whether or not foreclosure is probable.

Where, in the course of the orderly realisation of a loan it is exchanged for equity shares or properties, the exchange is accounted for as the sale of the loan and the acquisition of equity securities or investment properties. Where the Group's interest in equity shares following the exchange is such that the Group controls the entity, that entity is consolidated.

1. Accounting policies (continued)

o) Impairment of financial assets (continued)

Impairment losses are assessed individually for financial assets that are individually significant and individually or collectively for assets that are not individually significant. In making a collective assessment of impairment, financial assets are grouped into portfolios on the basis of similar risk characteristics. Future cash flows from these portfolios are estimated on the basis of the contractual cash flows and historical loss experience for assets with similar credit risk characteristics. Historical loss experience is adjusted, on the basis of current observable data, to reflect current conditions not affecting the period of historical experience.

Impairment losses are recognised in profit or loss and the carrying amount of the financial asset or group of financial assets reduced by establishing an allowance for impairment losses. If in a subsequent period the amount of the impairment loss reduces and the reduction can be ascribed to an event after the impairment was recognised, the previously recognised loss is reversed by adjusting the allowance. Once an impairment loss has been recognised on a financial asset or group of financial assets, interest income is recognised on the carrying amount using the original effective rate of interest at which estimated future cash flows were discounted in measuring impairment.

Impaired loans and receivables are written off, i.e. the impairment provision is applied in writing down the loan's carrying value partially or in full, when the Group concludes that there is no longer any realistic prospect of recovery of part or all of the loan. For loans that are individually assessed for impairment, the timing of write off is determined on a case-by-case basis. Such loans are reviewed regularly and write offs will be prompted by bankruptcy, insolvency, restructuring and similar events. Amounts recovered after a loan has been written off are credited to the loan impairment charge for the period in which they are received. Further details are given in Note 24 in the credit risk section.

Financial assets carried at fair value - when a decline in the fair value of a financial asset classified as available-for-sale has been recognised directly in other comprehensive income and there is objective evidence that it is impaired, the cumulative loss is reclassified from equity to profit or loss. The loss is measured as the difference between the amortised cost (including any hedge accounting adjustments) of the financial asset and its current fair value. Impairment losses on available-for-sale equity instruments are not reversed through profit or loss, but those on available-for-sale debt instruments are reversed, if there is an increase in fair value that is objectively related to a subsequent event.

p) Financial liabilities

On initial recognition financial liabilities, as defined by IAS 39, are recognised at fair value and classified into held-for-trading; designated as at fair value through profit or loss; or amortised cost.

Held-for-trading - a financial liability is classified as held-for-trading if it is incurred principally for the repurchase in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative (not in a qualifying hedge relationship). Held-for-trading financial liabilities are recognised at fair value with transaction costs being recognised in profit or loss. Subsequently they are measured at fair value. Gains and losses are recognised in profit or loss as they arise.

Designated as at fair value through profit or loss - financial liabilities may be designated as at fair value through profit or loss only if such designation (a) eliminates or significantly reduces a measurement or recognition inconsistency; or (b) applies to a group of financial assets, financial liabilities or both that the Group manages and evaluates on a fair value basis; or (c) relates to an instrument that contains an embedded derivative which is not evidently closely related to the host contract.

Financial liabilities that the Group designates on initial recognition as being at fair value through profit or loss are recognised at fair value, with transaction costs being recognised in profit or loss, and are subsequently measured at fair value. Gains and losses on financial liabilities that are designated as at fair value through profit or loss are recognised in profit or loss as they arise.

Amortised cost - all other financial liabilities are measured at amortised cost using the effective interest method (see accounting policy d).

Fair value – the Group’s approach to determining the fair value of financial instruments measured at fair value is set out in the section of critical accounting policies and key sources of estimation uncertainty entitled Fair value - financial instruments; further details are provided in Note 9.

1. Accounting policies (continued)

q) Derecognition

A financial asset is derecognised when the contractual right to receive cash flows from the asset has expired or when it has been transferred and the transfer qualifies for derecognition. A transfer requires that the Group either: (a) transfers the contractual rights to receive the asset's cash flows; or (b) retains the rights to the asset's cash flows but assumes a contractual obligation to pay those cash flows to a third party. After a transfer, the Group assesses the extent to which it has retained the risks and rewards of ownership of the transferred asset. If substantially all the risks and rewards have been retained, the asset remains on the balance sheet. If substantially all of the risks and rewards have been transferred, the asset is derecognised. If substantially all the risks and rewards have been neither retained nor transferred, the Group assess whether or not it has retained control of the asset. If it has not retained control, the asset is derecognised. Where the Group has retained control of the asset, it continues to recognise the asset to the extent of its continuing involvement.

A financial liability is removed from the balance sheet when the obligation is discharged, or cancelled, or expires. On the redemption or settlement of debt securities (including subordinated liabilities) issued by the Group, the Group derecognises the debt instrument and records a gain or loss being the difference between the debt's carrying amount and the cost of redemption or settlement.

The same treatment applies where the debt is exchanged for a new debt issue that has terms substantially different from those of the existing debt. The assessment of whether the terms of the new debt instrument are substantially different takes into account qualitative and quantitative characteristics including a comparison of the discounted present value of the cash flows under the new terms with the discounted present value of the remaining cash flows of the original debt issue.

r) Securitisation of residential mortgages

In accordance with the requirements of IFRS 10, the Group consolidates securitisation entities in which it does not hold voting rights but where it does retain the majority of the residual ownership risks and rewards in respect of interests in mortgages initially issued by the Bank and subsequently sold to the securitisation entities. The legal structure of the transactions involve the issue of senior and junior debt securities and subordinated loans by the securitisation entities and the establishment of deferred consideration as a function to remit excess returns generated by the securitisation entities to the Bank.

The Bank retains the risks and rewards of ownership of the mortgages through the acquisition of junior debt securities and subordinated debt that constitute credit enhancements for the senior debt securities and is entitled to deferred consideration. Therefore the mortgages are not derecognised from the balance sheet of the Bank. When the Bank has an asset to which it is contractually entitled under the terms of the transaction or a contractual liability these are recognised in full in the balance sheet of the Bank. Income and costs are recognised in profit or loss on an accruals basis.

Senior and junior debt securities are recognised in the Bank balance sheet as debt securities. Assets in respect of the subordinated debt and deferred consideration are recognised in the Bank balance sheet as loans and advances to customers. Liabilities due to the securitisation entities in respect of the cash flows from the underlying mortgages are recognised as customer deposits in the Bank balance sheet. The assets are classified as loans and receivables and measured at amortised cost under IAS 39. The liabilities are classified as at amortised cost.

As the securitisation entities are included in the Group's financial position under IFRS 10 all transactions and balances between the Bank and securitisation entities are fully eliminated on consolidation in the Group financial statements.

s) Sale and repurchase transactions

Securities subject to a sale and repurchase agreement under which substantially all the risks and rewards of ownership are retained by the Group continue to be shown on the balance sheet and the sale proceeds recorded as a deposit. Securities acquired in reverse sale and repurchase transactions under which the Group is not exposed to substantially all the risks and rewards of ownership are not recognised on the balance sheet and the consideration is recorded in loans and advances to banks or loans and advances to customers as appropriate.

Securities borrowing and lending transactions are usually secured by cash or securities advanced by the borrower. Borrowed securities are not recognised on the balance sheet or lent securities derecognised. Cash collateral received or given is treated as a loan or deposit; collateral in the form of securities is not recognised. However, where securities borrowed are transferred to third parties, a liability for the obligation to return the securities to the stock lending counterparty is recorded.

1. Accounting policies (continued)

t) Netting

Financial assets and financial liabilities are offset and the net amount presented in the balance sheet when, and only when, the Group has a legally enforceable right to set off the recognised amounts; and it intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously. The Group is party to a number of arrangements, including master netting agreements that give it the right to offset financial assets and financial liabilities. Where it does not intend to settle the amounts net or simultaneously the assets and liabilities concerned are presented gross.

u) Capital instruments

The Group classifies a financial instrument that it issues as a financial asset, financial liability or an equity instrument in accordance with the substance of the contractual arrangement. An instrument is classified as a liability if it is a contractual obligation to deliver cash or another financial asset, or to exchange financial assets or financial liabilities on potentially unfavourable terms. An instrument is classified as equity if it evidences a residual interest in the assets of the Group after the deduction of liabilities.

v) Derivatives and hedging

Derivative financial instruments are initially recognised, and subsequently measured, at fair value. Derivative fair values are determined from quoted prices in active markets where available. Where there is no active market for an instrument, fair value is derived from prices for the derivative's components using appropriate pricing or valuation models. Credit valuation adjustments are made when valuing derivative financial assets to incorporate counterparty credit risk. Valuation adjustments are made when fair valuing financial liabilities to reflect the Group's own credit standing.

A derivative embedded in a contract is accounted for as a stand-alone derivative if its economic characteristics are not closely related to the economic characteristics of the host contract; unless the entire contract is measured at fair value with changes in fair value recognised in profit or loss.

Gains and losses arising from changes in the fair value of derivatives that are not the hedging instrument in a qualifying hedge are recognised as they arise in profit or loss.

The Group enters into hedge relationships in respect of changes in the fair value of a recognised asset or liability or unrecognised firm commitment (fair value hedges).

Fair value hedge
In a fair value hedge, the gain or loss on the hedging instrument is recognised in profit or loss. The gain or loss on the hedged item attributable to the hedged risk is recognised in profit or loss and, where the hedged item is measured at amortised cost, adjusts the carrying amount of the hedged item. Hedge accounting is discontinued if the hedge no longer meets the criteria for hedge accounting; or if the hedging instrument expires or is sold, terminated or exercised; or if hedge designation is revoked. If the hedged item is one for which the effective interest rate method is used, any cumulative adjustment is amortised to profit or loss over the life of the hedged item using a recalculated effective interest rate.

Hedge relationships are formally designated and documented at inception. The documentation identifies the hedged item and the hedging instrument and details the risk that is being hedged and the way in which effectiveness will be assessed at inception and during the period of the hedge. If the hedge is not highly effective in offsetting changes in fair values attributable to the hedged risk, consistent with the documented risk management strategy, hedge accounting is discontinued. Hedge accounting is also discontinued if the Group revokes the designation of a hedged relationship.

w) Share-based payments

RBS Group awards options over shares to its employees and employees of subsidiary companies (including the Group) under various share option schemes. IFRS 2 'Share-based Payment' is applied by RBS Group to grants made under these schemes. The cost of employee services received in exchange for an award of shares or share options granted is measured by reference to the fair value of the shares or share options on the date the award is granted. The fair value of options granted is estimated using valuation techniques which incorporate exercise price, term, risk-free interest rates, the current share price and its expected volatility. The cost is expensed on a straight-line basis over the vesting period. RBS Group includes the cost of these awards in determining any recharges of employee costs it makes to subsidiaries. The Group recognises the cost based on these recharges.

x) Cash and cash equivalents

In the cash flow statements, cash and cash equivalents comprise cash and demand deposits with banks together with short-term highly liquid investments that are readily convertible to known amounts of cash and subject to insignificant risk of change in value.

1. Accounting policies (continued)

y) Investments in Group undertakings

The Bank's investments in its subsidiaries are stated at cost less any accumulated impairment losses.

z) Critical accounting policies and key sources of estimation uncertainty

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Irish company law and IFRS require the directors, in preparing the Group's financial statements, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. In the absence of an applicable standard or interpretation, IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors', requires management to develop and apply an accounting policy that results in relevant and reliable information in light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB's Conceptual Framework.

The judgements and assumptions involved in the Group's accounting policies that are considered by the Board to be the most important to the portrayal of its financial condition are discussed below. The use of estimates, assumptions or models that differ from those adopted by the Group would affect its reported results.

Loan impairment provisions

The Group's loan impairment provisions are established to recognise incurred impairment losses in its portfolio of loans classified as loans and receivables and carried at amortised cost. Loans (including lending under revolving facilities) with an impairment provision are reported as impaired. This includes loans granted forbearance where there is an economic loss and therefore an impairment provision.

There are three components to the Group's loan impairment provisions: individual, collective and latent.

Individual component - all impaired loans that exceed specific thresholds are individually assessed for impairment. Individually assessed loans principally comprise the Group's portfolio of commercial loans to medium and large businesses. Impairment losses are recognised as the difference between the carrying value of the loan and the discounted value of management's best estimate of future cash repayments and proceeds from any security held. These estimates take into account the customer's debt capacity and financial flexibility; the level and quality of its earnings; the amount and sources of cash flows; the industry in which the counterparty operates; and the realisable value of any security held. Estimating the quantum and timing of future recoveries involves significant judgement. The size of receipts will depend on the future performance of the borrower and the value of security, both of which will be affected by future economic conditions; additionally, collateral may not be readily marketable. The actual amount of future cash flows and the date they are received may differ from these estimates and consequently actual losses incurred may differ from those recognised in these financial statements.

Collective component - impaired loans that are below individual assessment thresholds are collectively assessed. Collectively assessed provisions are established on a portfolio basis using a present value methodology taking into account the level of arrears, security, past loss experience, credit scores and defaults based on portfolio trends. The most significant factors in establishing these provisions are the expected loss rates and the related average life. These portfolios include personal advances including mortgages, smaller commercial loans and credit card receivables. The future credit quality of these portfolios is subject to uncertainties that could cause actual credit losses to differ materially from reported loan impairment provisions. These uncertainties include the economic environment, notably interest rates and their effect on customer spending, the unemployment level, payment behaviour and bankruptcy trends.

Latent component – Latent component - latent loss provisions are held against estimated impairment losses in the performing portfolio that have yet to be identified as at the balance sheet date. To assess the latent loss within its portfolios, the Group has developed methodologies to estimate the time that an asset can remain impaired within a performing portfolio before it is identified and reported as such.

The impact of changes to significant inputs / assumptions during the financial year are discussed in Note 24.

Non-performing loans

Loans are considered to be non-performing if they are categorised as Risk Elements in Lending (REiL) or potential problem loans.

REiL comprises impaired loans and accruing loans past due 90 days or more. Accruing loans past due 90 days or more comprise loans past due 90 days where no impairment loss is expected. An asset is past due when any amount of interest, principal or fee has not been paid at the date it was due.

Potential problem loans are loans for which an impairment event has taken place but no impairment loss is expected. This category is used for advances which have met a pre-defined trigger for an impairment assessment and that assessment has determined that the future expected cash flows are greater than the carrying value of the asset.

1. Accounting policies (continued)

z) Critical accounting policies and key sources of estimation uncertainty (continued)

Forbearance

Forbearance takes place when a concession is made on the contractual terms of a loan in response to a customer's financial difficulties.

The forbearance policies are the main response to managing mortgage customers in financial difficulty and are deployed through the Group's forbearance initiative. While payment plans are provided to unsecured customers, forbearance is applied to secured retail products where relief is offered through the renegotiation of the original contract, although on terms not generally available on a commercial basis. This may include offering contract revision by various means including reduced repayment, interest only arrangements, negative amortisation, payment moratorium, term extensions, lifetime reduced repayment and/or interest rate reduction; these forbearance arrangements are subject to heightened monitoring.

Forbearance offered by the Group on loans where an impairment loss provision has been previously recognised will result in such loans retaining their classification as non-performing. Where the customer met the loan terms prior to modification and there is a realistic expectation that the customer will adhere to forbearance terms, these loans may in certain restricted circumstances (including appropriate consideration of probation periods) be classified as performing loans. In recognising their credit risk profile, they carry a provision incorporating an expectation that some customers will fail to comply with the terms of the forbearance together with the associated loss rate.

Deferred tax

The Group makes provision for deferred tax on short-term and other temporary differences where tax recognition occurs at a different time from accounting recognition. Tax assets are recognised in respect of unused tax losses to the extent that it is probable that there will be future taxable profits against which the losses can be utilised. Judgement is required to determine the amount of deferred tax assets that can be recognised, based on the likely timing and level of future taxable profits. Further details about the Group's deferred tax are provided in Note 19.

Pensions

There are three defined benefit pension schemes in operation within the Group: Ulster Bank Pension Scheme (Republic of Ireland), First Active Pension Scheme and Lombard Ireland Limited Non-Contributory Pension and Death Benefit Plan. The assets of defined benefit schemes are measured at their fair value at the balance sheet date. Scheme liabilities are measured using the projected unit method, which takes account of projected earnings increases, using actuarial assumptions that give the best estimate of the future cash flows that will arise under the scheme liabilities. These cash flows are discounted at an interest rate based on the yields of high-quality corporate bonds of appropriate duration, with high-quality almost universally understood to mean AA-rated. The choice of discount rate is a source of estimation uncertainty, due to a lack of appropriate Euro-denominated AA-rated bonds of equivalent duration to the pension schemes' liabilities.

The approach used is to fit a yield curve to an appropriate dataset of AA bonds, and derive the discount rate from that curve. To increase the number of reference bonds available at the end of the reporting period, equivalent AA yields were extrapolated for longer dated A and AAA rated bonds by applying a credit spread adjustment to their actual yields. These were then included in the dataset used to create the yield curve.

In determining the value of scheme liabilities, financial and demographic assumptions are made as to price inflation, pension increases, earnings growth and employee life expectancy. A range of assumptions could be adopted in valuing the schemes' liabilities. Different assumptions could significantly alter the amount of the surplus or deficit recognised in the balance sheet and the pension cost charged to the income statement. The assumptions adopted for the Group's pension schemes are set out in Note 5 together with sensitivities of the balance sheet and income statement to changes in those assumptions.

Fair value – financial instruments

Financial instruments classified as held-for-trading or designated as at fair value through profit or loss and financial assets classified as available-for-sale are recognised in the financial statements at fair value. All derivatives are measured at fair value. On the balance sheet, financial assets carried at fair value are included within equity shares and derivatives. Financial liabilities carried at fair value are included within deposits by banks, customer accounts and derivatives. Derivative assets and derivative liabilities are shown separately on the face of the balance sheets. The carrying value of a financial asset or a financial liability carried at cost or amortised cost that is the hedged item in a qualifying hedge relationship is adjusted by the gain or loss attributable to the hedged risk.

1. Accounting policies (continued)

z) Critical accounting policies and key sources of estimation uncertainty (continued)

Fair value – financial instruments (continued)

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair values are determined by reference to observable market prices where available and reliable. Where representative market prices for an instrument are not available or are unreliable because of poor liquidity, the fair value is derived from prices for its components using appropriate pricing or valuation models that are based on independently sourced market parameters, including interest rate yield curves, option volatilities and currency rates. Financial assets carried at fair value include government and corporate debt securities, reverse repos, loans, corporate equity shares and derivatives. Financial liabilities carried at fair value include deposits, repos, debt securities issued and derivatives. Fair value for a substantial proportion of these instruments is based on observable market prices or derived from observable market parameters. Where observable prices are not available, fair value is based on appropriate valuation techniques or management estimates.

The Group's derivative products include swaps, forwards, futures and options. Exchange traded instruments are valued using quoted prices. The fair value of over-the-counter instruments is derived from pricing models which take account of contract terms, including maturity, as well as quoted market parameters such as interest rates and volatilities. Values established from pricing models are adjusted for credit risk, liquidity risk and future operational costs.

The fair value of substantially all securities positions carried at fair value is determined directly from quoted prices. Fair value for a net open position in a financial instrument in an active market is the number of units of the instrument held times the closing market price. In determining the fair value of derivative financial instruments gross long and short positions measured at current mid market prices are adjusted by bid-offer reserves calculated on a portfolio basis. Credit valuation adjustments are made when valuing derivative financial assets to incorporate counterparty credit risk. Valuation adjustments are made when fair valuing financial liabilities to reflect the Group's own credit standing. Where the market for a financial instrument is not active, fair value is established using a valuation technique. These valuation techniques involve a degree of estimation, the extent of which depends on the instrument's complexity and the availability of market-based data.

More details about the Group's valuation methodologies of the fair value of financial instruments valued using techniques where at least one significant input is unobservable are provided in Note 9.

Provisions for liabilities

Provisions are liabilities of uncertain timing or amount, and are recognised when there is a present obligation as a result of a past event, the outflow of economic benefit is probable and the outflow can be estimated reliably. Judgement is involved in determining whether an obligation exists, and in estimating the probability, timing and amount of any outflows. Where the Group can look to another party such as an insurer to pay some or all of the expenditure required to settle a provision, any reimbursement is recognised when, and only when, it is virtually certain that it will be received. The provisions are management's best estimate of the anticipated costs of redress and related administration expenses. Further details on the Group's provisions for liabilities are provided in Note 18.

aa) Accounting developments

International Financial Reporting Standards

A number of IFRSs and amendments to IFRS were in issue at 31 December 2017 that would affect the Group from 1 January 2018 or later.

Effective 1 January 2018 - IFRS 9

In July 2014, the IASB published IFRS 9 'Financial Instruments' with an effective date of 1 January 2018. IFRS 9 replaces the current financial instruments standard IAS 39, setting out new accounting requirements in a number of areas.

The principle features of IFRS 9 are as follows:

Recognition and derecognition
The material in IAS 39 setting out the criteria for the recognition and derecognition of financial instruments have been included unamended in IFRS 9.

1. Accounting policies (continued)

aa) Accounting developments (continued)

Classification and measurement
Financial assets - there are three classifications for financial assets in IFRS 9.

Amortised cost - financial assets with terms that give rise to interest and principal cash flows only and which are held in a business model whose objective is to hold financial assets to collect their cash flow are measured at amortised cost.

Fair value through other comprehensive income - financial assets with terms that give rise to interest and principal cash flows only and which are held in a business model whose objective is achieved by holding financial assets to collect their cash flow and selling them are measured at fair value through other comprehensive income.

Fair value through profit and loss - other financial assets are measured at fair value through profit and loss.

At initial recognition, any financial asset may be irrevocably designated as measured at fair value through profit or loss if such designation eliminates a measurement or recognition inconsistency.

The measurement basis of the majority of the Group's financial assets will be unchanged on application of IFRS 9.

Financial liabilities - since early adopting in 2016 the IFRS 9 accounting for fair value attributable to own credit risk there are no further material changes on accounting for financial liabilities on adoption of IFRS 9.

Hedge accounting
IFRS 9's hedge accounting requirements are designed to align accounting more closely to the risk management framework; permit a greater variety of hedging instruments; and remove or simplify some of the rule-based requirements in IAS 39. The elements of hedge accounting: fair value, cash flow and net investment hedges are retained. The Group accounting policy choice is to continue with the IAS 39 hedge accounting framework.

Credit impairment
IFRS 9's credit impairment requirements apply to financial assets measured at amortised cost, to those measured at fair value through other comprehensive income, to lease receivables and to certain loan commitments and financial guarantee contracts. On initial recognition a loss allowance is established at an amount equal to 12-month expected credit losses (ECL) that is the portion of life-time expected losses resulting from default events that are possible within the next 12 months. Where a significant increase in credit risk since initial recognition is identified, the loss allowance increases so as to recognise all expected default events over the expected life of the asset. The Group expects that financial assets where there is objective evidence of impairment under IAS 39 will be credit impaired under IFRS 9, and carry loss allowances based on all expected default events.

The assessment of credit risk and the estimation of ECL are required to be unbiased and probability-weighted: determined by evaluating at the balance sheet date for each customer or loan portfolio a range of possible outcomes using reasonable and supportable information about past events, current conditions, forecasts of future events and economic conditions. The estimation of ECL also takes into account the discount of future cash flows. Recognition and measurement of credit impairments under IFRS 9 are more forward-looking than under IAS 39.

An RBS Group-wide programme has implemented the necessary changes in the modelling of credit loss parameters, and the underlying credit management and financial processes. The result is an increase in overall credit impairment provisions when compared with the current basis of measurement under IAS 39.

Transition
The Group will implement IFRS 9 'Financial instruments' on 1 January 2018. In terms of shareholders' equity, its current estimate of the opening balance sheet adjustment is to increase credit impairment provisions by €94m before tax. Changes in respect of classification and measurement are immaterial. This results in a net decrease in shareholders' equity, after tax, of €94m, including the impact of write-offs.

The increase in credit impairment provisions is partially offset by a reduction in the regulatory expected loss deduction, so is anticipated to result in a €26m (unaudited) reduction in CET1 capital. The changes in respect of classification and measurement are immaterial.

1. Accounting policies (continued)

aa) Accounting developments (continued)

Effective 1 January 2018 – other standards
IFRS 15 ‘Revenue from Contracts with Customers’ was issued in May 2014. It will replace IAS 11 ‘Construction Contracts’, IAS 18 ‘Revenue’ and several Interpretations. Contracts are bundled or unbundled into distinct performance obligations with revenue recognised as the obligations are met.

The Group has also adopted IFRS 15 Revenue from contracts with customers from 1 January 2018; it is not expected to have a material impact on shareholders’ equity.

IFRS 2 ‘Share-based payment’ was amended in June 2016 to clarify the accounting for net settlement of tax in respect of share-based payments and the calculation of the cost of modified awards and those with vesting conditions that are not market conditions.

IFRIC Interpretation 22 ‘Foreign Currency Transaction and Advance Consideration’ was issued in December 2016 clarifying the date of a foreign exchange transaction to be used on initial recognition of a related asset or other item.

IAS 40 ‘Investment Property’ was amended in December 2016 to clarify that transfers into or out of the investment property classification may only occur on a change of use or the property ceasing to meet the definition of an investment property.

Effective after 2018 – other standards
IFRS 16 ‘Leases’ was issued in January 2016 to replace IAS 17 ‘Leases’. There are no substantial changes to the accounting for leases by lessors. For lessees: accounting for finance leases will remain substantially the same; operating leases will be brought on balance sheet through the recognition of assets representing the contractual rights of use and liabilities will be recognised for the contractual payments. The effective date is 1 January 2019.

IFRS 17 ‘Insurance contracts’ was issued in May 2017 to replace IFRS 4 and to establish a comprehensive standard for inceptors of insurance policies. The effective date is 1 January 2021.

IFRIC Interpretation 23 ‘Uncertainty over income tax treatments’ was issued in June 2017 to clarify how to apply judgement in assessing the tax position of the reporting entity. The effective date is 1 January 2019.

In October 2017, the IASB amended IAS 28 ’Investments in associates and joint ventures’ to require long term, non-equity interests in these investments to be tested for impairment first in accordance with IFRS 9 and then in accordance with IAS 28. The effective date of the amendment is 1 January 2019.

The Group is assessing the effect of adopting these standards on its financial statements.

2. Net interest income

	Group	
	2017	2016
	€m	€m
Loans and advances to customers	**545**	580
Interest receivable	**545**	580
Customer accounts	**(25)**	(39)
Deposits by banks	**(16)**	(25)
Debt securities in issue	**(1)**	(2)
Subordinated liabilities	**(5)**	(6)
Interest payable on liabilities	**(47)**	(72)
Loans and advances to banks	**(17)**	(13)
Debt security assets	**(10)**	(6)
Interest payable on assets	**(27)**	(19)
Total interest payable	**(74)**	(91)
Net interest income	**471**	489

Included within net interest income is €29m (2016: €46m) of interest on impaired loans.

3. Non-interest income

	Group	
	2017	2016
	€m	€m
Fees and commission receivable		
Payment services	**34**	33
Credit and debit card fees	**29**	30
Lending (credit facilities)	**35**	36
Brokerage	**11**	9
Investment management	**5**	4
	114	112
Fees and commission payable	**(9)**	(15)
Income from trading activities[1]**:**		
Foreign exchange	**15**	11
Interest rates	**7**	46
Changes in fair value of own debt and derivative liabilities attributable to own credit	**(4)**	4
Equities and other	**4**	-
	22	61
Other operating income:		
Profit on disposal of loans and receivables	**10**	6
Loss on redemption of subordinated debt	**(9)**	**-**
Other income	**10**	13
	11	19
Non-interest income	**138**	177

(1) The analysis of trading income is based on how the business is organised and the underlying risks managed.
Trading income comprises gains and losses on financial instruments held-for-trading, both realised and unrealised, net interest and dividends and the related funding costs.
i) Foreign exchange: spot foreign exchange contracts, currency swaps and options, emerging markets and related hedges and funding.
ii) Interest rates: interest rate swaps, forward foreign exchange contracts, forward rate agreements, interest rate options, interest rate futures and related hedges and funding.
iii) Equities and other: equities and equity derivatives.

4. Operating expenses

	Group	
	2017	2016
	€m	€m
Wages, salaries and other staff costs	**150**	165
Social security costs	**17**	18
Pension costs:		
- defined benefit schemes (see Note 5)	**32**	43
- defined contribution schemes (see Note 5)	**3**	3
Restructure costs	**18**	12
Staff costs	**220**	241
Premises and equipment	**50**	19
Administration	**427**	502
Other expenses	**477**	521
Property, plant and equipment depreciation and impairment (see Note 15)	**12**	10
Operating expenses	**709**	772

Included within administration costs is €192m (2016: €198m) in respect of conduct provisions.

The average number of persons employed by the Group during the financial year, excluding temporary staff was 2,491 (2016: 2,566). The average number of temporary employees during 2017 was 209 (2016: 105). The number of persons employed by the Group at 31 December, excluding temporary staff, was as follows:

	Group	
	2017	2016
Employee numbers	**Number**	Number
Retail Banking	**1,011**	1,168
Commercial Banking	**334**	418
Other	**992**	1,025
	2,337	2,611

	Group	
	2017	2016
Auditor's remuneration	**€'000**	€'000
Audit of the Bank's individual and Group accounts	**1,670**	1,173
Other assurance services	**45**	185
	1,715	1,358

The figures in the auditor's remuneration table relate to fees payable to the statutory auditor, exclusive of VAT.

Other than the amounts disclosed above, no remuneration was payable in respect of tax advisory services and other non-audit services.

5. Pension costs

Pension risk is the risk to the Group arising from its contractual or other liabilities to, or with respect to, its pension schemes, whether established for its employees, for those of a related company or otherwise.

As set out in Note 24 on the financial statements, the Group is exposed to risk from its defined benefit pension schemes to the extent that the assets of the schemes do not fully match the timing and amount of the schemes' liabilities. Pension scheme liabilities vary with changes to long-term interest rates, inflation, pensionable salaries and the longevity of scheme members as well as changes in legislation. The Group is exposed to the risk that the market value of the schemes' assets, together with future returns and any additional future contributions could be considered insufficient to meet the liabilities as they fall due. In such circumstances, the Group could be obliged, or may choose, to make additional contributions to the schemes or be required to hold additional capital to mitigate such risk.

The Group operates the following defined benefit pension schemes, the assets of which are independent of the Group's finances:

Name of schemes
Ulster Bank Pension Scheme (Republic of Ireland) ("UBPS")
First Active Pension Scheme
Lombard Ireland Limited Non-Contributory Pension and Death Benefit Plan

The Group's main pension scheme, UBPS, operates under Irish trust law and is managed and administered on behalf of its members in accordance with the terms of the trust deed, scheme rules and Irish legislation (principally the Pensions Act 1990). Under Irish legislation a defined benefit pension scheme is required to build up and maintain enough funds to pay members their pension entitlements should the scheme be wound up. Pension fund trustees are required to obtain regular actuarial valuations and reports put in place a recovery plan addressing any funding shortfall and submit that plan to the Irish Pensions Authority for approval.

The corporate trustee of the UBPS is Ulster Bank Pension Trustees (RI) Limited ("UBPTRIL"), a wholly owned subsidiary of the Bank. UBPTRIL is the legal owner of the scheme assets which are held separately from the assets of the Group. The board of UBPTRIL comprises 2 trustee directors nominated by the unions and 7 appointed by the Group. The board is responsible for operating the scheme in line with its formal rules and pensions law. It has a duty to act in the best interests of all scheme members, including pensioners and those who are no longer employed by the Group, but who still have benefits in the scheme. Similar governance principles apply to the other two schemes.

The schemes were closed to new entrants beyond 2010, when new defined contribution schemes were launched.

Employees make contributions at varying levels depending on which scheme they are a member of and when they joined the scheme. In addition, employees may make voluntary contributions to secure additional benefits on a money-purchase basis.

The Group also make contributions to a small number of RBS Group pension schemes, the costs of which are accounted for as defined contributions.

The Group independently monitors risk within its pension funds as part of the Internal Capital Adequacy Assessment Process. The UBIDAC Pension Committee, set up in 2017, acts as a sub-committee of the UBIDAC Executive Committee and formulates the view of pension risk; considering mechanisms that could potentially be used for managing risk within the scheme as well as financial strategy, and also reviews actuarial assumptions from a sponsor perspective as appropriate. Oversight is also provided by the RBS Pension Committee.

In the Republic of Ireland, the Trustees of defined benefit pension schemes are required to perform funding valuations every three years. The Trustees and the Company, with the support of the Scheme Actuary, agree the assumptions used to value the liabilities and a Schedule of Contributions required to eliminate any funding deficit. The funding assumptions incorporate a margin for prudence over and above the expected cost of providing the benefits promised to members, taking into account the sponsor's covenant and the investment strategy of the scheme. The last funding valuation of the main scheme was at 31 December 2015 and the next funding valuation is due at 31 December 2018. A special contribution of €200m was made to the UBPS in March 2017, putting the scheme into a surplus position and removing the requirement for the funding plan agreed at the last triennial valuation. The funding plan for the First Active Pension Scheme remains in place for €6.8m p.a. until 2020 (increasing in line with inflation each year). For both schemes contingent asset arrangements have been put in place to cover the Risk Reserve requirements arising under the Minimum Funding Standard framework.

A funding plan was put in place for the Lombard scheme during 2016 which requires contributions of €1.65m p.a. until 2025.

The Group made contributions of €3m to its defined contribution schemes in 2017 (2016: €3m).

5. Pension costs (continued)

Interim valuations of the Group's pension schemes were prepared to 31 December 2017 by independent actuaries, using the following assumptions:

	Group and Bank	
Principal actuarial assumptions at 31 December (weighted average)	**2017**	2016
Discount rate	**2.20%**	2.00%
Rate of increase in salaries	**1.50%-2.75%**	1.30%-2.50%
Rate of increase in pensions in payment	**0.00%-1.85%**	0.00%-1.60%
Inflation assumption	**1.75%**	1.50%

Discount rate

The Euro yield curve is constructed by reference to yields on 'AA' corporate bonds from which a single discount rate is derived based on a cash flow profile similar in structure and duration to the pension obligations. Significant judgement is required when setting the criteria for bonds to be included in the population from which the yield curve is derived. The criteria include issuance size, quality of pricing and the exclusion of outliers. Judgement is also required in determining the shape of the yield curve at long durations: a constant credit spread relative to gilts is assumed.

	Group and Bank	
Major classes of plan assets as a percentage of total plan assets	**2017**	2016
Quoted assets		
Quoted equities	**27%**	40%
Government fixed interest bonds	**8%**	2%
Corporate and other bonds	**32%**	28%
Unquoted assets		
Private equity	**2%**	2%
Hedge funds	**2%**	-
Real estate	**3%**	4%
Derivatives	**5%**	11%
Cash and other assets	**21%**	13%

	Group and Bank	
Post–retirement mortality assumptions (Main scheme)	**2017**	2016
Longevity for current pensioners currently aged 70 (years)		
Males	**17.8**	17.6
Females	**19.2**	19.1
Longevity for future pensioners currently aged 63 (years)		
Males	**24.3**	24.1
Females	**26.0**	25.9

These post-retirement mortality assumptions are derived from standard mortality tables used by the scheme actuary to value the liabilities for the main scheme.

	2017	2016
Amounts recognised on the balance sheet	**€m**	€m
Net assets of schemes in surplus	**62**	-
Net liabilities of schemes in deficit	**(11)**	(244)
	51	(244)

5. Pension costs (continued)

	Group and Bank		
Changes in value of net pension asset	**Fair value of plan assets €m**	**Present value of defined benefit obligations €m**	**Net pension (liability)/asset €m**
At 1 January 2017	**1,354**	**(1,598)**	**(244)**
Income statement:			
Net interest cost	30	(32)	**(2)**
Current service cost	-	(29)	**(29)**
Past service cost	-	(1)	**(1)**
	30	(62)	**(32)**
Statement of comprehensive income:			
Return on plan assets above recognised interest income	48	-	**48**
Experience gains and losses	-	18	**18**
Effect of changes in actuarial financial assumptions	-	21	**21**
Effect of changes in actuarial demographic assumptions	-	6	**6**
	48	45	**93**
Contributions by employer	234	-	**234**
Contributions by plan participants	2	(2)	**-**
Benefits paid	(45)	45	**-**
At 31 December 2017	**1,623**	**(1,572)**	**51**

	Group and Bank		
Changes in value of net pension liability	**Fair value of plan assets €m**	**Present value of defined benefit obligations €m**	**Net pension liability €m**
At 1 January 2016	1,069	(1,456)	(387)
Income statement:			
Net interest cost	32	(41)	(9)
Current service cost	-	(30)	(30)
Past service cost	-	(4)	(4)
	32	(75)	(43)
Statement of comprehensive income:			
Return on plan assets above recognised interest income	79	-	79
Experience gains and losses	-	48	48
Effect of changes in actuarial financial assumptions	-	(62)	(62)
Effect of changes in actuarial demographic assumptions	-	48	48
	79	34	113
Inter group transfers	120	(144)	(24)
Contributions by employer	97	-	97
Contributions by plan participants	2	(2)	-
Benefits paid	(45)	45	-
At 31 December 2016	1,354	(1,598)	(244)

The Group expects to contribute €25m to its defined benefit pension schemes in 2018.

The weighted average duration of the Group's defined benefit obligation is 22 years (2016: 24 years).

5. Pension costs (continued)

History of defined benefit schemes (Group and Bank)	2017 €m	2016 €m	2015 €m	2014 €m	2013 €m
Present value of defined benefit obligations	**(1,572)**	(1,598)	(1,456)	(1,650)	(1,156)
Fair value of plan assets	**1,623**	1,354	1,069	1,062	878
Net surplus/(deficit)	**51**	(244)	(387)	(588)	(278)
Experience gains on plan liabilities	**18**	48	15	12	54
Experience gains/(losses) on plan assets	**48**	79	(26)	129	(9)
Actual return on pension scheme assets	**78**	111	(2)	162	26

The table below sets out the sensitivities of the pension cost for the financial year and the present value of defined benefit obligations at the balance sheet dates to a change in the principal actuarial assumptions:

	Group and Bank			
	(Decrease)/increase in pension cost for the year		(Decrease)/increase in obligation at 31 December	
	2017 €m	2016 €m	**2017 €m**	2016 €m
0.25% increase in the discount rate	**(4)**	(4)	**(86)**	(88)
0.25% increase in inflation	**1**	2	**30**	41
0.25% additional rate of increase in pensions in payment	**-**	2	**19**	19
0.25% additional rate of increase in deferred pensions	**-**	1	**21**	22
0.25% additional rate of increase in salaries	**2**	2	**19**	20
Longevity increase of 1 year	**2**	2	**44**	39

6. Emoluments of directors

	2017 €	2016 €
Emoluments for the provision of directors' services	**1,583,885**	1,325,291
Contributions and allowances in respect of pension schemes	**69,384**	40,474
Emoluments relating to long-term incentive schemes	**151,101**	300,519
Total emoluments received	**1,804,370**	1,666,284

Retirement benefits were accruing to one director under defined contribution schemes at the year end (2016: one). No retirement benefits were accruing to directors under defined benefit schemes at the year end or previous year end.

No share options were exercised during the year that resulted in gains to directors (2016: none).

Performance related bonuses are awarded to executive directors on the basis of measuring annual performance against certain specified financial targets, which include both corporate performance objectives and key strategic objectives.

During the financial year there were no emoluments in respect of compensation payments for loss of office (2016: €nil).

During the year the highest paid director received emoluments of €917,661 (2016: €665,656).

The executive directors may also participate in the RBS executive share option and Sharesave schemes.

There were no amounts paid or payable to third parties during the financial year or the preceding financial year in respect of making available the services of any person as a director of the Bank or any of its subsidiaries or otherwise in connection with the management of the Group's affairs.

7. Taxation

	Group	
	2017	2016
Current taxation:	**€m**	€m
Corporation Tax at 12.5% (2016: 12.5%)		
Credit/(charge) for the financial year	**2**	(1)
Deferred taxation:		
Credit/(charge) for the financial year	**4**	(6)
Over provision in respect of prior periods	**-**	6
Increase in deferred tax asset in respect of previously unrecognised losses	**-**	6
Total deferred taxation	**4**	6
Tax credit for the financial year	**6**	5

The actual tax credit differs from the expected tax credit/(charge) computed by applying the standard rate of Irish Corporation Tax of 12.5% (2016: 12.5%) as follows:

	2017	2016
	€m	€m
Operating (loss)/profit before tax	**(168)**	32
Tax credit/(charge) on operating (loss)/profit at the standard rate	**21**	(4)
Factors affecting the charge for the financial year:		
Tax arising at rates other than the standard rate of tax	**(17)**	29
Temporary differences	**(2)**	(15)
Non-deductible items	**(3)**	(61)
Non-taxable income	**33**	-
Deferred tax not recognised on current year losses	**(26)**	-
Losses brought forward and utilised	**-**	44
Increase in deferred tax asset in respect of previously unrecognised losses	**-**	6
Adjustments to tax credit in respect of prior periods	**-**	6
Actual tax credit for the financial year	**6**	5

8. Profit/loss dealt with in the financial statements of the Bank

In accordance with the exemption contained within Section 304 of the Companies Act 2014 the primary financial statements of the Bank do not include an income statement or statement of comprehensive income. The Bank's loss after tax for the year ended 31 December 2017 was €151m (2016: €380m profit).

9. Financial instruments

The following tables analyse the financial assets and financial liabilities of the Group and Bank in accordance with the categories of financial instruments as defined by IAS 39. Assets and liabilities outside the scope of IAS 39 are shown within non financial assets/liabilities.

	Group						
	Held-for-trading	Designated as at fair value through profit or loss	Available-for-sale	Loans and receivables	Amortised cost	Non financial assets / liabilities	Total
2017	€m	€m	€m	€m	€m	€m	€m
Assets							
Cash and balances at central banks	-	-	-	322	-	-	322
Loans and advances to banks[1]	-	-	-	4,893	-	-	4,893
Loans and advances to customers[2]	-	-	-	21,950	-	-	21,950
Debt securities	-	-	2,038	-	-	-	2,038
Equity shares	-	-	5	-	-	-	5
Derivatives	582	-	-	-	-	-	582
Intangible assets	-	-	-	-	-	1	1
Property, plant and equipment	-	-	-	-	-	72	72
Prepayments, accrued income and other assets	-	-	-	-	-	35	35
Retirement benefit assets	-	-	-	-	-	62	62
Deferred taxation	-	-	-	-	-	285	285
Assets held for sale	-	-	-	-	-	3	3
	582	-	2,043	27,165	-	458	30,248
Liabilities							
Deposits by banks[3]	341	-	-	-	2,154	-	2,495
Customer accounts[4]	-	689	-	-	19,128	-	19,817
Derivatives	439	-	-	-	-	-	439
Provisions, accruals and other liabilities	-	-	-	-	-	467	467
Retirement benefit liabilities	-	-	-	-	-	11	11
Subordinated liabilities	-	-	-	-	616	-	616
	780	689	-	-	21,898	478	23,845
Equity							6,403
							30,248

For notes relating to this table refer to page 45.

9. Financial instruments (continued)

	Group						
2016	Held-for-trading €m	Designated as at fair value through profit or loss €m	Available-for-sale €m	Loans and receivables €m	Amortised cost €m	Non financial assets / liabilities €m	Total €m
Assets							
Cash and balances at central banks	-	-	-	290	-	-	290
Loans and advances to banks[1]	-	-	-	4,622	-	-	4,622
Loans and advances to customers[2]	-	-	-	22,014	-	-	22,014
Debt securities	-	-	2,340	-	-	-	2,340
Equity shares	-	-	6	-	-	-	6
Derivatives	1,025	-	-	-	-	-	1,025
Property, plant and equipment	-	-	-	-	-	78	78
Prepayments, accrued income and other assets	-	-	-	-	-	26	26
Deferred taxation	-	-	-	-	-	293	293
	1,025	-	2,346	26,926	-	397	30,694
Liabilities							
Deposits by banks[3]	28	-	-	-	1,647	-	1,675
Customer accounts[4]	-	1,089	-	-	17,865	-	18,954
Debt securities in issue[5]	-	-	-	-	1,377	-	1,377
Derivatives	886	-	-	-	-	-	886
Provisions, accruals and other liabilities	-	-	-	-	-	351	351
Retirement benefit liabilities	-	-	-	-	-	244	244
Subordinated liabilities	-	-	-	-	719	-	719
	914	1,089	-	-	21,608	595	24,206
Equity							6,488
							30,694

(1) Includes reverse repurchase agreements of €861m (2016: €360m) and items in the course of collection from other banks of €38m (2016: €35m).

(2) The Group has advances secured on residential property subject to non-recourse funding. Under IAS 39, these securitised mortgages qualify for full recognition on the balance sheet at 31 December 2017 and are included in loans and advances to customers. As at 31 December 2017 €6,814m (2016: €9,992m) is included in loans and advances to customers.

(3) The Group holds €8m (2016: €28m) of cash and securities received as collateral in respect of derivative assets. There are no other financial instruments that are subject to IAS 32 (on balance sheet) netting arrangements or subject to enforceable master netting instruments or similar agreements that are not set off in accordance with IAS 32.

(4) The carrying amount of customer accounts designated as at fair value through profit or loss is €83m higher (2016: €99m) than the principal amount. No amounts have been recognised (2016: €nil) in profit or loss for changes in credit risk associated with these liabilities.

(5) Comprised of bonds and medium term notes €1,377m. The medium term notes that were issued by limited recourse entities controlled by the Bank and collateralised on residential mortgages held by the Bank were fully redeemed at par during the financial year.

9. Financial instruments (continued)

	Bank						
2017	Held-for-trading €m	Designated as at fair value through profit or loss €m	Available-for-sale €m	Loans and receivables €m	Amortised cost €m	Non financial assets / liabilities €m	Total €m
Assets							
Cash and balances at central banks	-	-	-	322	-	-	322
Loans and advances to banks [1]	-	-	-	4,893	-	-	4,893
Loans and advances to customers [2]	-	-	-	22,364	-	-	22,364
Debt securities[3]	-	-	2,038	5,281	-	-	7,319
Equity shares	-	-	5	-	-	-	5
Investments in Group undertakings	-	-	-	-	-	5	5
Derivatives	554	-	-	-	-	-	554
Intangible assets	-	-	-	-	-	1	1
Property, plant and equipment	-	-	-	-	-	71	71
Prepayments, accrued income and other assets	-	-	-	-	-	34	34
Retirement benefit assets	-	-	-	-	-	62	62
Deferred taxation	-	-	-	-	-	285	285
Assets held for sale	-	-	-	-	-	3	3
	554	-	2,043	32,860	-	461	35,918
Liabilities							
Deposits by banks [4]	341	-	-	-	2,153	-	2,494
Customer accounts [5]	-	689	-	-	24,833	-	25,522
Derivatives	204	-	-	-	-	-	204
Provisions, accruals and other liabilities	-	-	-	-	-	465	465
Retirement benefit liabilities	-	-	-	-	-	11	11
Subordinated liabilities	-	-	-	-	616	-	616
	545	689	-	-	27,602	476	29,312
Equity							6,606
							35,918

For notes relating to this table refer to page 47.

9. Financial instruments (continued)

	Bank						
	Held-for-trading	Designated as at fair value through profit or loss	Available-for-sale	Loans and receivables	Amortised cost	Non financial assets / liabilities	Total
2016	€m	€m	€m	€m	€m	€m	€m
Assets							
Cash and balances at central banks	-	-	-	290	-	-	290
Loans and advances to banks [(1)]	-	-	-	4,303	-	-	4,303
Loans and advances to customers [(2)]	-	-	-	22,499	-	-	22,499
Debt securities[(3)]	-	-	2,340	7,731	-	-	10,071
Equity shares	-	-	6	-	-	-	6
Investments in Group undertakings	-	-	-	-	-	16	16
Derivatives	986	-	-	-	-	-	986
Property, plant and equipment	-	-	-	-	-	77	77
Prepayments, accrued income and other assets	-	-	-	-	-	26	26
Deferred taxation	-	-	-	-	-	293	293
	986	-	2,346	34,823	-	412	38,567
Liabilities							
Deposits by banks [(4)]	28	-	-	-	1,646	-	1,674
Customer accounts[(5)]	-	1,089	-	-	27,460	-	28,549
Derivatives	351	-	-	-	-	-	351
Provisions, accruals and other liabilities	-	-	-	-	-	351	351
Retirement benefit liabilities	-	-	-	-	-	244	244
Subordinated liabilities	-	-	-	-	719	-	719
	379	1,089	-	-	29,825	595	31,888
Equity							6,679
							38,567

(1) Includes reverse repurchase agreements of €861m (2016: €360m) and items in the course of collection from other banks of €38m (2016: €35m).

(2) The Bank has advances secured on residential property subject to non-recourse funding. Under IAS 39, these securitised mortgages qualify for full recognition on the balance sheet at 31 December 2017 and are included in loans and advances to customers. As at 31 December 2017 €6,814m (2016: €9,992m) is included in loans and advances to customers.

(3) Of the debt securities balance above, the Bank had pledged €236m (2016: €236m) of the debt securities to RBS plc as collateral against intraday SEPA payments which RBS plc processes on behalf of the Bank. A further €20m (2016: €60m) of debt securities were pledged as collateral to UBPS and €17m (2016: €nil) of debt securities were pledged as collateral to the trustees of First Active Pension Scheme under contingent asset arrangements put in place to cover the Risk Reserve requirements arising under the Minimum Funding Standard framework. The debt securities classified as loans and receivables in the Bank have been issued by limited recourse entities that are controlled by the Bank. The securities are collateralised on the cash flows of residential mortgages held by the Bank, are long term in nature and generate variable interest, typically at mark-ups over Euro Interbank Offer Rates. The carrying value of the instruments is not considered to be impaired as at 31 December 2017 and 31 December 2016 and represents the full extent of the credit risk on the instruments.

(4) The Bank holds €8m (2016: €28m) of cash and securities received as collateral in respect of derivative assets. There are no other financial instruments that are subject to IAS 32 (on balance sheet) netting arrangements or subject to enforceable master netting instruments or similar agreements that are not set off in accordance with IAS 32.

(5) The carrying amount of other customer accounts designated as at fair value through profit or loss is €83m higher (2016: €99m) than the principal amount.

9. Financial instruments (continued)

Valuation of financial instruments carried at fair value

Control environment
The Group places reliance on the independent price verification (IPV) process of NatWest Markets, a division of the RBS Group, and eliminates its market risk on its trading book portfolios by entering into back to back positions with RBS plc.

The Group's control environment for the determination of the fair value of financial instruments includes formalised protocols for the review and validation of fair values independent of the businesses entering into the transactions. There are specific controls to ensure consistent pricing policies and procedures, incorporating disciplined price verification. The Group ensures that appropriate attention is given to structured products, illiquid products and other instruments which are difficult to price.

Common valuation policies, procedures, frameworks and models apply across the Group.

Independent price verification
IPV is a key element of the control environment. Valuations may be directly from available prices, or may be derived using a model and variable model inputs. These valuations are reviewed, and if necessary amended, by a team independent of those trading the financial instruments in the light of available pricing evidence.

IPV differences are classified according to the quality of independent market observables into IPV quality bands linked to the fair value hierarchy principles, as laid out in IFRS 13 'Fair Value Measurement'. These differences are classified into fair value levels 1, 2 and 3 (with the valuation uncertainty risk increasing as the levels rise from 1 to 3) and then further classified into high, medium, low and indicative depending on the quality of the independent data available to validate the prices. Valuations are revised if they are outside agreed thresholds.

Governance framework
IPV takes place at least each month end date, for exposures in the trading book and at least quarterly for exposures in the banking book. The IPV control includes formalised reporting and escalation of any valuation differences in breach of established thresholds. The Pricing Unit determines IPV policy, monitors adherence to that policy and performs additional independent reviews of highly subjective valuation issues. The quality and completeness of the information gathered in the IPV process gives an indication as to the liquidity and valuation uncertainty of an instrument.

Valuation hierarchy
These classifications of financial instruments are reviewed and challenged by management and are also subject to senior management review. Particular attention is paid to instruments crossing from one level to another, new instrument classes or products, instruments that are generating significant profit and loss and instruments where valuation uncertainty is high.

Valuation techniques
The Group derives the fair value of its instruments differently depending on whether the instrument is a non-modelled or a modelled product.

Non-modelled products
Non-modelled products are valued directly from a price input typically on a position by position basis.

Modelled products
Modelled products valued using a pricing model range in complexity from comparatively vanilla products such as interest rate swaps and forwards through to more complex derivatives. The valuation of modelled products requires an appropriate model and inputs into this model. Sometimes models are also used to derive inputs (e.g. to construct volatility surfaces). The Group uses a number of modelling methodologies.

Inputs to valuation models
Values between and beyond available data points are obtained by interpolation and extrapolation. When utilising valuation techniques, the fair value can be significantly affected by the choice of valuation model and by underlying assumptions concerning factors such as the amounts and timing of cash flows, discount rates and credit risk. The principal inputs to these valuation techniques are as follows:

Bond prices - quoted prices are generally available for government bonds, certain corporate securities and some mortgage-related products.

Credit spreads - where available, these are derived from prices of credit default swaps or other credit based instruments, such as debt securities. For others, credit spreads are obtained from pricing services. For counterparty credit spreads, adjustments are made to market prices (or parameters) when the creditworthiness of the counterparty differs from that of the assumed counterparty in the market price (or parameters).

Interest rates - these are principally benchmark interest rates such as the London Interbank Offered Rate (LIBOR), European Interbank Offered Rate (EURIBOR), Overnight Index Swaps (OIS) rate and other quoted interest rates in the swap, bond and futures markets.

9. Financial instruments (continued)

Foreign currency exchange rates - there are observable prices both for spot and forward contracts and futures in the world's major currencies.

Equity and equity index prices - quoted prices are generally readily available for equity shares listed on the world's major stock exchanges and for major indices on such shares.

Price volatilities and correlations - volatility is a measure of the tendency of a price to change with time. Correlation measures the degree which two or more prices or other variables are observed to move together.

Prepayment rates - the fair value of a financial instrument that can be prepaid by the issuer or borrower differs from that of an instrument that cannot be prepaid. In valuing prepayable instruments that are not quoted in active markets, the Group considers the value of the prepayment option.

Recovery rates/loss given default - these are used as an input to valuation models and reserves for asset-backed securities and other credit products as an indicator of severity of losses on default. Recovery rates are primarily sourced from market data providers or inferred from observable credit spreads.

Valuation
When valuing financial instruments in the trading book, adjustments are made to mid-market valuations to cover bid-offer spread, liquidity and credit risk.

Valuation of financial instruments in the banking books are made to the mid-price.

Credit valuation adjustments
Credit valuation adjustments (CVA) represent an estimate of the adjustment to fair value that a market participant would make to incorporate the counterparty credit risk inherent in derivative exposures. CVA at 31 December 2017 was €1m (2016: €2m).

The CVA is calculated on a portfolio basis reflecting an estimate of the amount a third party would charge to assume the credit risk.

Where a positive exposure exists to a counterparty that is considered to be close to default, the CVA is calculated by applying expected losses to the current level of exposure. Otherwise, expected losses are applied to estimated potential future positive exposures which are modelled to reflect the volatility of the market factors which drive the exposures and the correlation between those factors.

Expected losses are determined from market implied probabilities of default and internally assessed recovery levels. The probability of default is calculated with reference to observable credit spreads and observable recovery levels. For counterparties where observable data do not exist, the probability of default is determined from the credit spreads and recovery levels of similarly rated entities.

Collateral held under a credit support agreement is factored into the CVA calculation. In such cases where the Group holds collateral against counterparty exposures, CVA is held to the extent that residual risk remains.

Debt valuation adjustments
The fair value of the Group’s derivative financial liabilities is adjusted to reflect the Group’s own credit risk through debt valuation adjustments (DVA). Expected gains are applied to estimated potential future negative exposures, the modelling of which is consistent with the approach used in the calculation of CVA. Expected gains are determined from market implied probabilities of default and recovery levels. Funding valuation adjustment (FVA) is considered the primary adjustment applied to derivative liabilities. The extent to which DVA and FVA overlap is eliminated from DVA.

9. Financial instruments (continued)

The following tables show the financial instruments carried at fair value by valuation method:

	Group							
	2017				2016			
	Level 1 (1)	**Level 2 (2)**	**Level 3 (3)**	**Total**	Level 1 (1)	Level 2 (2)	Level 3 (3)	Total
	€m	**€m**	**€m**	**€m**	€m	€m	€m	€m
Assets								
Debt securities	**1,558**	**480**	**-**	**2,038**	2,340	-	-	2,340
Equity shares	**-**	**-**	**5**	**5**	-	-	6	6
Derivatives	**-**	**303**	**279**	**582**	-	596	429	1,025
Total	**1,558**	**783**	**284**	**2,625**	2,340	596	435	3,371
Liabilities								
Deposits by banks	**-**	**341**	**-**	**341**	-	28	-	28
Customer accounts	**-**	**689**	**-**	**689**	-	1,089	-	1,089
Derivatives	**-**	**169**	**270**	**439**	-	311	575	886
Total	**-**	**1,199**	**270**	**1,469**	-	1,428	575	2,003

	Bank							
	2017				2016			
	Level 1 (1)	**Level 2 (2)**	**Level 3 (3)**	**Total**	Level 1 (1)	Level 2 (2)	Level 3 (3)	Total
	€m	**€m**	**€m**	**€m**	€m	€m	€m	€m
Assets								
Debt securities	**1,558**	**480**	**-**	**2,038**	2,340	-	-	2,340
Equity shares	**-**	**-**	**5**	**5**	-	-	6	6
Derivatives	**-**	**303**	**251**	**554**	-	596	390	986
Total	**1,558**	**783**	**256**	**2,597**	2,340	596	396	3,332
Liabilities								
Deposits by banks	**-**	**341**	**-**	**341**	-	28	-	28
Customer accounts	**-**	**689**	**-**	**689**	-	1,089	-	1,089
Derivatives	**-**	**169**	**35**	**204**	-	311	40	351
Total	**-**	**1,199**	**35**	**1,234**	-	1,428	40	1,468

(1) Valued using unadjusted quoted prices in active markets for identical financial instruments. This category includes government securities.

(2) Valued using techniques based significantly on observable market data. Instruments in this category are valued using:
a) quoted prices for similar instruments or identical instruments in markets which are not considered to be active; or
b) valuation techniques where all the inputs that have a significant effect on the valuation are directly or indirectly based on observable market data.
The type of instruments that trade in markets that are not considered to be active, but are based on quoted market prices, broker dealer quotations or alternative pricing sources with reasonable levels of price transparency and those instruments valued using techniques include most government agency securities, investment-grade corporate bonds, certain mortgage products, certain bank and bridge loans, repos and reverse repos, less liquid equities, state and municipal obligations, most physical commodities, certain money market securities and loan commitments and most Over-the-counter ("OTC") derivatives.

(3) Instruments in this category have been valued using a valuation technique where at least one input (which could have a significant effect on the instrument's valuation) is not based on observable market data. Where inputs can be observed from market data without undue cost and effort, the observed input is used. Otherwise, the Group determines a reasonable level for the input.
Financial instruments included within level 3 of the fair value hierarchy primarily consist of OTC derivatives where valuation depends upon unobservable inputs such as certain credit and exotic derivatives. No gain or loss is recognised on the initial recognition of a financial instrument valued using a technique incorporating significant unobservable data.

Included within the level 3 derivative assets and liabilities of the Group and Bank are balance guaranteed swaps in respect of securitisation transactions. These instruments are priced taking contractual principal schedule of underlying loans through a model which allows for the impact of the correlation between various market variables (interest rates and floating rate tenor basis) and varying prepayment speeds to be modelled. The model works on the premise that prepayment levels (or Constant Prepayment Rate – CPR) are negatively correlated with interest rates, meaning that more loan holders will repay when these variables are low. The model is sensitive to the estimate of future CPR which is not an observable input. If prepayments were 1% higher than expected, this would cause a movement of €8m in the value of these swaps.

9. Financial instruments (continued)

Level 3 portfolio movement tables

	Group					
	Equity shares		Derivative assets		Derivative liabilities	
	2017	2016	**2017**	2016	**2017**	2016
	€m	€m	**€m**	€m	**€m**	€m
At 1 January	**6**	7	**429**	291	**(575)**	(360)
Disposals	**(1)**	(1)	**-**	-	**-**	-
(Charge)/credit to income statement	**-**	-	**(150)**	138	**305**	(215)
At 31 December	**5**	6	**279**	429	**(270)**	(575)

	Bank					
	Equity shares		Derivative assets		Derivative liabilities	
	2017	2016	**2017**	2016	**2017**	2016
	€m	€m	**€m**	€m	**€m**	€m
At 1 January	**6**	7	**390**	215	**(40)**	(77)
Disposals	**(1)**	(1)	**-**	-	**-**	-
(Charge)/credit to income statement	**-**	-	**(139)**	175	**5**	37
At 31 December	**5**	6	**251**	390	**(35)**	(40)

The following tables show the carrying values and the fair values of financial instruments on the balance sheet carried at amortised cost. The fair value of cash and balances at central banks and €2,438m of loans and advances to banks carried at amortised cost (2016: €2,606m) have been determined using procedures consistent with the requirements of level 2 valuation methodologies, as set out on page 50. All other balances have been fair valued using procedures that fall within level 3 of the fair value methodologies.

	Group			
	2017 Carrying value	**2017 Fair value**	2016 Carrying value	2016 Fair value
	€m	**€m**	€m	€m
Financial assets				
Cash and balances at central banks	**322**	**322**	290	290
Loans and advances to banks	**4,893**	**4,893**	4,622	4,622
Loans and advances to customers	**21,950**	**20,029**	22,014	19,487
Financial liabilities				
Deposits by banks	**2,154**	**2,154**	1,647	1,647
Customer accounts	**19,128**	**19,131**	17,865	17,873
Debt securities in issue	**-**	**-**	1,377	1,129
Subordinated liabilities	**616**	**573**	719	591

9. Financial instruments (continued)

	Bank			
	2017	**2017**	2016	2016
	Carrying value	**Fair value**	Carrying value	Fair value
	€m	**€m**	€m	€m
Financial assets				
Cash and balances at central banks	**322**	**322**	290	290
Loans and advances to banks	**4,893**	**4,893**	4,303	4,303
Loans and advances to customers	**22,364**	**20,443**	22,499	19,972
Debt securities	**5,281**	**4,135**	7,731	6,414
Financial liabilities				
Deposits by banks	**2,153**	**2,153**	1,646	1,646
Customer accounts	**24,833**	**24,836**	27,460	27,467
Subordinated liabilities	**616**	**573**	719	591

Fair value calculation

The fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Quoted market values are used where available, otherwise fair values have been estimated based on discounted expected future cash flows and other valuation techniques. These techniques involve uncertainties and require assumptions and judgements covering prepayments, credit risk and discount rates. Furthermore there is a wide range of potential valuation techniques. Changes in these assumptions would significantly affect estimated fair values. The fair values reported would not necessarily be realised in an immediate sale or settlement.

The assumptions and methodologies underlying the calculation of fair values of financial instruments at the balance sheet date are as follows:

Short-term financial instruments and loans and advances to banks

For loans and advances to banks and certain short-term financial instruments: cash and balances at central banks, items in the course of collection from other banks, settlement balances, items in the course of transmission to other banks, demand deposits and notes in circulation, fair value approximates to carrying value.

Loans and advances to customers

In estimating the fair value of loans and advances to customers measured at amortised cost, the Group's loans are segregated into appropriate portfolios reflecting the characteristics of the constituent loans. The principal method used to estimate fair value in the Group is to discount expected cash flows at the current offer rate for the same or similar products.

For certain portfolios where there are very few or no recent transactions bespoke approaches are utilised.

Debt securities

The majority of debt securities are valued using quoted prices in active markets, or using quoted prices for similar assets in active markets. Fair values of the rest are determined using discounted cash flow valuation techniques.

Deposits by banks and customer accounts

Fair values of deposits are estimated using discounted cash flow valuation techniques.

Debt securities in issue and subordinated liabilities

Fair values are determined using quoted prices for similar liabilities where available or by reference to valuation techniques, adjusting for own credit spreads where appropriate.

9. Financial instruments (continued)

Remaining maturity

	Group		
	Less than 12 months	**More than 12 months**	**Total**
2017	**€m**	**€m**	**€m**
Assets			
Cash and balances at central banks	**322**	**-**	**322**
Loans and advances to banks	**4,892**	**1**	**4,893**
Loans and advances to customers	**2,749**	**19,201**	**21,950**
Debt securities	**1,312**	**726**	**2,038**
Equity shares	**-**	**5**	**5**
Derivatives	**141**	**441**	**582**
Liabilities			
Deposits by banks	**1,992**	**503**	**2,495**
Customer accounts	**18,755**	**1,062**	**19,817**
Derivatives	**29**	**410**	**439**
Subordinated liabilities	**-**	**616**	**616**

	Group		
	Less than 12 months	More than 12 months	Total
2016	€m	€m	€m
Assets			
Cash and balances at central banks	290	-	290
Loans and advances to banks	4,546	76	4,622
Loans and advances to customers	2,773	19,241	22,014
Debt securities	1,391	949	2,340
Equity shares	-	6	6
Derivatives	181	844	1,025
Liabilities			
Deposits by banks	168	1,507	1,675
Customer accounts	17,846	1,108	18,954
Debt securities in issue	-	1,377	1,377
Derivatives	85	801	886
Subordinated liabilities	-	719	719

	Bank		
	Less than 12 months	**More than 12 months**	**Total**
2017	**€m**	**€m**	**€m**
Assets			
Cash and balances at central banks	**322**	**-**	**322**
Loans and advances to banks	**4,892**	**1**	**4,893**
Loans and advances to customers	**3,159**	**19,205**	**22,364**
Debt securities	**6,593**	**726**	**7,319**
Equity shares	**-**	**5**	**5**
Derivatives	**141**	**413**	**554**
Liabilities			
Deposits by banks	**1,991**	**503**	**2,494**
Customer accounts	**24,460**	**1,062**	**25,522**
Derivatives	**29**	**175**	**204**
Subordinated liabilities	**-**	**616**	**616**

9. Financial instruments (continued)

	Bank		
	Less than 12 months	More than 12 months	Total
2016	€m	€m	€m
Assets			
Cash and balances at central banks	290	-	290
Loans and advances to banks	4,227	76	4,303
Loans and advances to customers	3,255	19,244	22,499
Debt securities	9,122	949	10,071
Equity shares	-	6	6
Derivatives	181	805	986
Liabilities			
Deposits by banks	167	1,507	1,674
Customer accounts	27,441	1,108	28,549
Derivatives	85	266	351
Subordinated liabilities	-	719	719

10. Financial assets - impairment

The following table shows the movement in the provisions for impairment losses for loans and advances:

	Group and Bank			
	Individually assessed	**Collectively assessed**	**Latent**	**Total**
	€m	**€m**	**€m**	**€m**
At 1 January 2017	**80**	**1,222**	**90**	**1,392**
Currency translation and other adjustments	**-**	**(39)**	**-**	**(39)**
Amounts written-off[(1)]	**(30)**	**(111)**	**-**	**(141)**
Recoveries of amounts previously written-off	**8**	**5**	**-**	**13**
(Credit)/charge to the income statement	**(11)**	**84**	**(5)**	**68**
Unwind of discount (recognised in interest income)	**(1)**	**(28)**	**-**	**(29)**
At 31 December 2017 [(2)]	**46**	**1,133**	**85**	**1,264**

	Group and Bank			
	Individually assessed	Collectively assessed	Latent	Total
	€m	€m	€m	€m
At 1 January 2016	1,578	2,216	340	4,134
Currency translation and other adjustments	(47)	(22)	-	(69)
Amounts written-off[(1)]	(1,462)	(1,056)	-	(2,518)
Recoveries of amounts previously written-off	22	7	-	29
(Credit)/charge to the income statement	(9)	121	(250)	(138)
Unwind of discount (recognised in interest income)	(2)	(44)	-	(46)
At 31 December 2016 [(2)]	80	1,222	90	1,392

(1) Includes amounts relating to impairments previously recognised on assets included in sale transactions. Amounts written-off do not include any loans and advances to banks.
(2) Impairment provisions at 31 December 2017 and 31 December 2016 do not include any balances held against loans and advances to banks.

10. Financial assets - impairment (continued)

Loan impairment
The Group considers financial assets to be impaired when there is no longer a reasonable prospect of receiving the contractual cash flows in accordance with the contract and the net present value of any security is less than the outstanding amount.

The following table shows analysis of impaired financial assets:

	2017			2016		
Group and Bank	**Gross carrying value €m**	**Provision €m**	**Net book value €m**	Gross carrying value €m	Provision €m	Net book value €m
Impaired financial assets						
Loans and advances to customers	**3,244**	**(1,179)**	**2,065**	3,718	(1,302)	2,416
- of which are individually assessed	**65**	**(46)**	**19**	108	(80)	28

The following tables show total impairment provisions and past due and impaired assets on loans and advances to customers by geographic area:

	Group and Bank					
2017	**Impaired assets €m**	**Past due more than 90 days but not impaired assets €m**	**Individually and collectively assessed provisions €m**	**Latent provisions €m**	**Total provisions €m**	**Charge/(credit) to the income statement €m**
Geographic area [(1)]						
United Kingdom	**-**	**-**	**-**	**-**	**-**	**-**
Republic of Ireland	**3,244**	**442**	**1,179**	**85**	**1,264**	**68**
	3,244	**442**	**1,179**	**85**	**1,264**	**68**

2016	€m	€m	€m	€m	€m	€m
Geographic area [(1)]						
United Kingdom	5	-	1	-	1	1
Republic of Ireland	3,713	375	1,301	90	1,391	(139)
	3,718	375	1,302	90	1,392	(138)

(1) The analysis by geographic area is based on the location of the lender.

10. Financial assets - impairment (continued)

The following tables show total impairment provisions and past due and impaired assets on loans and advances to customers by industry sector:

	Group and Bank					
2017	**Impaired assets €m**	**Past due more than 90 days but not impaired assets €m**	**Individually and collectively assessed provisions €m**	**Latent provisions €m**	**Total provisions €m**	**(Credit)/ charge to the income statement €m**
Industry sector						
Agriculture and fisheries	**28**	**3**	**23**	**-**	**23**	**14**
Building and construction	**24**	**-**	**27**	**-**	**27**	**1**
Business services	**25**	**6**	**21**	**-**	**21**	**(41)**
Financial services	**11**	**-**	**10**	**-**	**10**	**1**
Manufacturing	**18**	**5**	**9**	**-**	**9**	**5**
Individuals	**3,038**	**422**	**1,010**	**-**	**1,010**	**81**
Power and water	**1**	**-**	**1**	**-**	**1**	**1**
Property	**37**	**4**	**32**	**-**	**32**	**(4)**
Public sector and quasi-government	**19**	**-**	**12**	**-**	**12**	**5**
Telecoms, media and technology	**2**	**-**	**2**	**-**	**2**	**1**
Tourism and leisure	**12**	**2**	**12**	**-**	**12**	**1**
Transport and storage	**6**	**-**	**4**	**-**	**4**	**-**
Wholesale and retail trade	**23**	**-**	**16**	**-**	**16**	**8**
Latent	**-**	**-**	**-**	**85**	**85**	**(5)**
	3,244	**442**	**1,179**	**85**	**1,264**	**68**

	Group and Bank					
2016	Impaired assets €m	Past due more than 90 days but not impaired assets €m	Individually and collectively assessed provisions €m	Latent provisions €m	Total provisions €m	(Credit)/ charge to the income statement €m
Industry sector						
Agriculture and fisheries	20	2	12	-	12	(8)
Building and construction	47	-	45	-	45	-
Business services	60	8	63	-	63	(128)
Financial services	16	-	13	-	13	(1)
Manufacturing	13	-	6	-	6	(5)
Individuals	3,454	279	1,073	-	1,073	284
Property	48	2	46	-	46	(39)
Public sector and quasi-government	14	81	10	-	10	-
Telecoms, media and technology	2	-	2	-	2	12
Tourism and leisure	16	-	16	-	16	(11)
Transport and storage	9	-	4	-	4	4
Wholesale and retail trade	19	3	12	-	12	4
Latent	-	-	-	90	90	(250)
	3,718	375	1,302	90	1,392	(138)

10. Financial assets - impairment (continued)

	Group and Bank	
	2017	2016
	€m	€m
Gross income not recognised at balance sheet date but which would have been recognised under the original terms of non–accrual and restructured loans:		
United Kingdom	**-**	1
Republic of Ireland	**259**	247
	259	248

The following assets were past due at the balance sheet date but not considered impaired:

Group and Bank	**Past due 1–29 days**	**Past due 30–59 days**	**Past due 60–89 days**	**Past due more than 90 days**	**Total**
2017	**€m**	**€m**	**€m**	**€m**	**€m**
Loans and advances to customers	**742**	**283**	**174**	**442**	**1,641**
2016					
Loans and advances to customers	763	301	217	375	1,656

11. Debt securities

	Group					
	2017			2016		
	Other central and local government	**Mortgage backed securities**	**Total**	Other central and local government	Mortgage backed securities	Total
	€m	**€m**	**€m**	€m	€m	€m
Available-for-sale	**2,038**	**-**	**2,038**	2,340	-	2,340

	Bank					
	2017			2016		
	Other central and local government	**Mortgage backed securities**	**Total**	Other central and local government	Mortgage backed securities	Total
	€m	**€m**	**€m**	€m	€m	€m
Available-for-sale	**2,038**	**-**	**2,038**	2,340	-	2,340
Loans and receivables	**-**	**5,281**	**5,281**	-	7,731	7,731
Total	**2,038**	**5,281**	**7,319**	2,340	7,731	10,071

The Group and Bank recorded net unrealised losses of €3m (2016: €2m gain) during the financial year.

The Bank holds €5,281m (2016: €7,731m) of mortgage backed securities issued by securitisation vehicles which are consolidated at the Group level.

During the financial year all of the mortgage backed securities issued by four securitisation vehicles were redeemed at par. These limited recourse entities were controlled by the Group and included in the consolidated financial statements on that basis. At 31 December 2016 the value of the mortgage backed securities issued by these four securitisation vehicles and held as assets by the Bank was €2,118m.

12. Equity shares

	Group and Bank	
	2017	2016
	Unlisted	Unlisted
	€m	€m
Available-for-sale	**5**	6

13. Investments in Group undertakings

Investments in Group undertakings are carried at cost less impairment. Movements during the year were as follows:

	Bank	
	2017	2016
	€m	€m
At 1 January	**16**	17
Dissolution of Group undertakings	**(9)**	-
Impairment	**(2)**	(1)
At 31 December	**5**	16

The €9m dissolution of Group undertakings reflects three subsidiary undertakings which were previously placed into members' voluntary liquidation and dissolved during the financial year.

The principal subsidiary undertaking of the Bank is shown below. Its capital consists of unlisted ordinary shares. This undertaking is owned directly and is wholly-owned.

Undertaking	Nature of business	Country of incorporation
Easycash (Ireland) Limited	Provision of ATMs in convenient locations	Republic of Ireland

All of the Group undertakings, as detailed in Note 33, are consolidated in the Group's financial statements and have an accounting reference date of 31 December.

14. Intangible assets

	Group and Bank
	€m
At 1 January 2017	**-**
Additions	**1**
At 31 December 2017	**1**
Accumulated amortisation and impairment:	
At 1 January 2017	**-**
Charge for period	**-**
At 31 December 2017	**-**
Carrying amount at 31 December 2017	**1**

Intangible assets are principally internally generated software.

15. Property, plant and equipment

	Group					
2017	**Investment properties €m**	**Freehold land and buildings €m**	**Leases of 50 years or more unexpired €m**	**Leases of 50 years or less unexpired €m**	**Computer and other equipment €m**	**Total €m**
Cost or valuation:						
At 1 January 2017	-	65	15	66	64	**210**
Additions	-	3	1	5	3	**12**
Transfer to asset held for sale	-	(4)	(2)	-	(1)	**(7)**
Disposals and write-off of fully depreciated assets	-	-	-	(5)	(11)	**(16)**
At 31 December 2017	**-**	**64**	**14**	**66**	**55**	**199**
Accumulated impairment, depreciation and amortisation:						
At 1 January 2017	-	30	14	38	50	**132**
Transfer to asset held for sale	-	(2)	(1)	-	(1)	**(4)**
Disposals and write-off of fully depreciated assets	-	-	-	(4)	(9)	**(13)**
Depreciation charge for the financial year	-	1	-	8	3	**12**
At 31 December 2017	**-**	**29**	**13**	**42**	**43**	**127**
Carrying amount at 31 December 2017	**-**	**35**	**1**	**24**	**12**	**72**

	Group					
2016	Investment properties €m	Freehold land and buildings €m	Leases of 50 years or more unexpired €m	Leases of 50 years or less unexpired €m	Computer and other equipment €m	Total €m
Cost or valuation:						
At 1 January 2016	15	68	15	65	62	225
Additions	-	2	-	1	2	5
Disposals and write-off of fully depreciated assets	(15)	(5)	-	-	-	(20)
At 31 December 2016	-	65	15	66	64	210
Accumulated impairment, depreciation and amortisation:						
At 1 January 2016	-	32	14	34	47	127
Disposals and write-off of fully depreciated assets	-	(5)	-	-	-	(5)
Impairment charge for the financial year	-	3	-	-	-	3
Depreciation charge for the financial year	-	-	-	4	3	7
At 31 December 2016	-	30	14	38	50	132
Carrying amount at 31 December 2016	-	35	1	28	14	78

There was no investment property held to generate rental income (2016: €nil) or incur direct operating expenses (2016: €nil).

15. Property, plant and equipment (continued)

	Bank					
2017	**Investment properties €m**	**Freehold land and buildings €m**	**Leases of 50 years or more unexpired €m**	**Leases of 50 years or less unexpired €m**	**Computer and other equipment €m**	**Total €m**
Cost or valuation:						
At 1 January 2017	-	64	9	66	61	**200**
Additions	-	3	1	5	3	**12**
Transfer to asset held for sale	-	(4)	(2)	-	(1)	**(7)**
Disposals and write-off of fully depreciated assets	-	-	-	(5)	(11)	**(16)**
At 31 December 2017	**-**	**63**	**8**	**66**	**52**	**189**
Accumulated impairment, depreciation and amortisation:						
At 1 January 2017	-	30	9	37	47	**123**
Transfer to asset held for sale	-	(2)	(1)	-	(1)	**(4)**
Disposals and write-off of fully depreciated assets	-	-	-	(4)	(9)	**(13)**
Depreciation charge for the financial year	-	1	-	8	3	**12**
At 31 December 2017	**-**	**29**	**8**	**41**	**40**	**118**
Carrying amount at 31 December 2017	**-**	**34**	**-**	**25**	**12**	**71**

	Bank					
2016	Investment properties €m	Freehold land and buildings €m	Leases of 50 years or more unexpired €m	Leases of 50 years or less unexpired €m	Computer and other equipment €m	Total €m
Cost or valuation:						
At 1 January 2016	2	67	9	65	59	202
Additions	-	2	-	1	2	5
Disposals and write-off of fully depreciated assets	(2)	(5)	-	-	-	(7)
At 31 December 2016	-	64	9	66	61	200
Accumulated impairment, depreciation and amortisation:						
At 1 January 2016	-	30	9	33	44	116
Disposals and write-off of fully depreciated assets	-	(3)	-	-	-	(3)
Impairment charge for the financial year	-	3	-	-	-	3
Depreciation charge for the financial year	-	-	-	4	3	7
At 31 December 2016	-	30	9	37	47	123
Carrying amount at 31 December 2016	-	34	-	29	14	77

There was no profit on disposal of freehold land and buildings in the Group or Bank during either financial year.

16. Derivatives

Companies in the Group transact derivatives as principal either as a trading activity or to manage balance sheet foreign exchange, interest rate and credit risk.

	Group					
	2017			2016		
	Notional amounts	**Assets**	**Liabilities**	Notional amounts	Assets	Liabilities
	€m	**€m**	**€m**	€m	€m	€m
Over-the counter derivatives						
Foreign exchange contracts:						
Spot, forwards and futures	**1,201**	**16**	**19**	1,735	54	44
Currency swaps	**745**	**39**	**39**	1,556	114	260
Interest rate contracts:						
Interest rate swaps	**29,808**	**436**	**381**	38,711	736	582
Options purchased	**32**	**-**	**-**	26	-	-
Options written	**33**	**-**	**-**	26	-	-
Equity and commodity contracts	**620**	**91**	**-**	1,052	121	-
	32,439	**582**	**439**	43,106	1,025	886

	Bank					
	2017			2016		
	Notional amounts	**Assets**	**Liabilities**	Notional amounts	Assets	Liabilities
	€m	**€m**	**€m**	€m	€m	€m
Over-the-counter derivatives						
Foreign exchange contracts:						
Spot, forwards and futures	**1,201**	**16**	**19**	1,735	54	44
Currency swaps	**745**	**39**	**39**	1,070	114	114
Interest rate contracts:						
Interest rate swaps	**25,337**	**408**	**146**	30,635	697	193
Options purchased	**32**	**-**	**-**	26	-	-
Options written	**33**	**-**	**-**	26	-	-
Equity and commodity contracts	**620**	**91**	**-**	1,052	121	-
	27,968	**554**	**204**	34,544	986	351

Included in the table above are derivatives held for hedging purposes as follows:

	Group & Bank					
	2017			2016		
	Notional amounts	**Assets**	**Liabilities**	Notional amounts	Assets	Liabilities
	€m	**€m**	**€m**	€m	€m	€m
Fair value hedging						
Interest rate contracts	**386**	**1**	**4**	395	1	4

Hedge ineffectiveness recognised in other operating income in continuing operations comprised:

	2017	2016
	€m	€m
Fair value hedging		
Gains on the hedged items attributable to the hedged risk	1	2
Losses on the hedging instruments	(1)	(2)
Fair value hedging ineffectiveness	**-**	-

17. Prepayments, accrued income and other assets

	Group		Bank	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
Prepayments	**5**	6	**5**	6
Accrued income	**7**	5	**7**	5
Other assets	**23**	15	**22**	15
	35	26	**34**	26

18. Provisions, accruals and other liabilities

	Group		Bank	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
Accruals	**64**	77	**63**	76
Deferred income	**7**	7	**7**	7
Provisions for liabilities and charges	**370**	236	**370**	236
Other liabilities	**26**	31	**25**	32
	467	351	**465**	351

The following amounts are included within provisions for liabilities and charges:

	Group and Bank						
	Tracker mortgage examination	**Other customer remediation**	**Litigation**	**Global restructuring group**	**Property**	**Other**	**Total**
	€m	**€m**	**€m**	**€m**	**€m**	**€m**	**€m**
At 1 January 2016	-	-	-	-	32	26	58
Transfer from accruals	5	-	9	-	-	-	14
Charge to income statement	206	-	6	11	2	8	233
Utilised in the year	(21)	-	-	-	(5)	(10)	(36)
Release to income statement	-	-	-	-	(19)	(14)	(33)
At 1 January 2017	190	-	15	11	10	10	236
Charge to income statement	87	100	4	-	15	7	213
Utilised in the year	(54)	(3)	(1)	(5)	(3)	-	(66)
Release to income statement	-	-	(2)	-	(4)	(7)	(13)
At 31 December 2017	**223**	**97**	**16**	**6**	**18**	**10**	**370**

18. Provisions, accruals and other liabilities (continued)

Tracker mortgage examination

In December 2015, the CBI announced that it had written to a number of lenders requiring them to put in place a robust plan and framework to review the treatment of customers who have been sold mortgages with a tracker interest rate or with a tracker interest rate entitlement. The CBI stated that the intended purpose of the review was to identify any cases where customers' contractual rights under the terms of their mortgage agreements were not fully honoured, or where lenders did not fully comply with various regulatory requirements and standards regarding disclosure and transparency for customers.

During the financial year the Group progressed its in-depth review and by 31 December 2017 1,038 customers had received remediation and compensation. The remainder are being contacted and remediated as quickly as possible. A charge of €87m (2016: €206m) has been recognised in the financial statements based on an updated assessment of remediation and project costs.

At 31 December 2017 the Group has recognised a provision of €223m (2016: €190m), bringing the total income statement charge since the review commenced to €298m. The Group expects that the majority of this provision will be utilised within 12 months. Due to the scale and complexity of the review a number of assumptions are inherent in the calculation of the provision which represents management's best estimate of expected remediation and project costs. Therefore the ultimate financial impact may be different from the amount provided.

Other customer remediation

As part of an internal review of the wider personal and commercial loan portfolios, extending from the tracker mortgage examination programme, the Group identified further legacy business issues. A programme is ongoing to identify and remediate impacted customers. Any issues relating to tracker mortgage products are included in the tracker mortgage examination provision as outlined above.

At 31 December 2017 the Group has recognised a provision of €97m (2016: €nil) based on management's best estimate of expected remediation and project costs relating to the above internal review. Pending completion of the Group's review there remains uncertainty as to the eventual cost of redress and associated project costs which will depend on final determination of the size of the impacted population and average redress costs. Assumptions relating to these are inherently uncertain and the ultimate financial impact may be different from the amount provided. The Group expects the majority of this provision to be utilised within the next 12 to 18 months.

Global restructuring group (GRG)

The Group holds a provision of €6m (2016: €11m) in respect of the FCA review of the treatment of SME customers, relating to the automatic refund of complex fees for SME customers that were in GRG between 2008 and 2013, additional redress costs arising from a new complaints process and the associated operational costs. Background information in relation to the FCA review of SME customers is given in Note 25. The Group expects the majority of this provision to be utilised within the next 12 months.

Property

The property provisions principally comprise provisions for onerous lease contracts. The timing for such payments is uncertain. Provision is made for future rentals payable in respect of vacant leasehold property and for any shortfall where leased property is sub-let at a rental lower than the lease rentals payable by the Group.

19. Deferred taxation

Provision for deferred taxation has been made as follows:

	Group and Bank			
	Pension	Accelerated capital allowances	Tax losses	Total
	€m	€m	€m	€m
At 1 January 2016	2	(1)	286	287
Credit to income statement	-	-	6	6
At 1 January 2017	2	(1)	292	293
Credit to income statement	4	-	-	4
Charge to other comprehensive income	(12)	-	-	(12)
At 31 December 2017	**(6)**	**(1)**	**292**	**285**

19. Deferred taxation (continued)

Deferred taxation on losses

A deferred tax asset of €292m (2016: €292m) has been recognised in respect of €2,333m (2016: €2,333m) of total tax losses of €9,684m (2016: €9,489m) carried forward at 31 December 2017. These losses arose principally from significant impairment losses reflecting weak economic conditions in the Republic of Ireland. The Irish economy continues to improve and, based on current business forecasts, the losses on which a deferred tax asset has been recognised will be materially recovered against future taxable profits of the company by the end of 2024. Under Irish tax legislation, tax losses do not expire and can be carried forward indefinitely.

20. Subordinated liabilities

	Group and Bank	
	2017	2016
	€m	€m
Dated loan capital	**530**	605
Undated loan capital	**86**	114
	616	719

	Group and Bank	
	2017	2016
	€m	€m
Dated loan capital		
€430m floating rate loan capital repayable 2022:[1]		
- held by NatWest Holdings (3 month EURIBOR plus 0.35%)	**430**	430
€100m floating rate loan capital repayable 2022:		
- held by RBS plc (3 month EURIBOR plus 0.35%)	**100**	100
€35m floating rate repayable 2020:		
- held by Ulster Bank Limited (3 month EURIBOR plus 0.4%)	**-**	35
€40m floating rate repayable 2019:		
- held by Ulster Bank Limited (3 month EURIBOR plus 0.5%)	**-**	40
	530	605
Undated loan capital		
€31m (2016: €38m) 11.375% perpetual tier two capital[2]	**55**	62
£11m (2016: £20m) 11.75% perpetual tier two capital[2]	**30**	40
£1.1m (2016: £1.3m) perpetual floating rate tier two capital (6 month sterling LIBOR plus 2.55%)[2]	**1**	2
£8m loan capital - held by Ulster Bank Limited	**-**	10
	86	114
Total	**616**	719

(1) The Bank may prepay the loan (in whole or in part) together with interest accrued to the date fixed for prepayment on the interest payment date falling in July 2017 or any interest payment date falling thereafter, provided that the CBI has approved the prepayment and a minimum 30 days notice is provided to the lender. During the year Ulster Bank Limited sold its holding of this subordinated note to NatWest Holdings.

(2) During the year €7m of the 11.375% undated loan capital, £9m of the 11.75% loan capital and £0.2m of the perpetual floating rate tier two capital in issue was redeemed following a tender offer. A €9m loss was recognised on redemption of these notes.

Claims in respect of the Bank's loan capital are subordinate to the claims of other creditors. None of the loan capital is secured.

Dated loan capital

Interest on the dated loan capital is payable quarterly at a margin over Euro Interbank Offer Rates (EURIBOR) as noted above.

Undated loan capital

The €31m, £11m and £1.1m subordinated perpetual bonds were issued by First Active Limited, in the Republic of Ireland, at par on conversion of First National Building Society to a public limited company pursuant to Section 107 of the Building Societies Act, 1989 to replace the issued fixed and floating rate permanent interest bearing shares of the Society. The issuance of the bonds transferred to the Bank when First Active Limited transferred its banking business in February 2010. The claims of the holders of the bonds are subordinate to the claims of all creditors of the Bank.

Interest on the £1.1m perpetual floating rate tier two capital is payable at a margin over London Interbank Offer Rates (LIBOR) as noted above.

21. Share capital presented as equity

	Group and Bank			
	Allotted, called up and fully paid		Authorised	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
Equity shares:				
Ordinary B shares of €1.27	**1,825**	1,825	**2,223**	2,223
Ordinary B shares of €1	**1,745**	1,745	**2,400**	2,400
Ordinary A shares of £1	**22**	22	**34**	34
Total share capital	**3,592**	3,592	**4,657**	4,657

	Allotted, called up and fully paid		Authorised	
	2017	2016	**2017**	2016
Number of shares	**Millions**	Millions	**Millions**	Millions
Equity shares:				
Ordinary B shares of €1.27	**1,437**	1,437	**1,750**	1,750
Ordinary B shares of €1	**1,745**	1,745	**2,400**	2,400
Ordinary A shares of £1	**15**	15	**25**	25
Total share capital	**3,197**	3,197	**4,175**	4,175

All share classes rank pari passu in all respects.

22. Leases

The Group provides asset finance to its customers through acting as a lessor. It purchases plant and equipment, renting them to customers under lease arrangements that, depending on their terms, qualify as either operating or finance leases.

Amounts receivable under finance lease and hire purchase agreements:

	Group and Bank					
	2017			2016		
	Gross amounts	**Present value adjustments**	**Present value**	Gross amounts	Present value adjustments	Present value
Year in which receipt will occur:	**€m**	**€m**	**€m**	€m	€m	€m
Within 1 year	**104**	**(6)**	**98**	89	(4)	85
After 1 year but within 5 years	**137**	**(12)**	**125**	97	(6)	91
After 5 years	**3**	**-**	**3**	2	-	2
	244	**(18)**	**226**	188	(10)	178

Future minimum amounts payable under non–cancellable operating leases:

	Group and Bank							
	2017				2016			
Year in which payment will occur:	**Within 1 year**	**After 1 year but within 5 years**	**After 5 years**	**Total**	Within 1 year	After 1 year but within 5 years	After 5 years	Total
	€m	**€m**	**€m**	**€m**	€m	€m	€m	€m
Operating lease obligations:								
Premises	**12**	**31**	**28**	**71**	14	34	21	69

22. Leases (continued)

	Group and Bank	
	2017	2016
	€m	€m
Amounts recognised in income statement		
Operating leases - minimum rentals payable	**14**	14

23. Collateral and securitisations

Securities repurchase agreements and lending transactions

The Group enters into securities repurchase agreements and securities lending transactions under which it receives or transfers cash or securities as collateral in accordance with normal practice. Generally, the agreements require additional collateral to be provided if the value of the securities fall below a predetermined level.

Under standard terms for repurchase transactions in the Republic of Ireland, the recipient of the collateral has an unrestricted right to sell or repledge it, subject to returning equivalent securities on settlement of the transaction.

There were no securities transferred under repurchase transactions included within debt securities on the balance sheet at 31 December 2017 and 31 December 2016. There were securities amounting to €861m received as collateral under reverse repurchase agreements at 31 December 2017 (2016: €360m).

Other collateral given

The Group pledges other collateral with its counterparties in respect of:

	Group		Bank	
	2017	**2016**	**2017**	2016
Group assets charged as security for liabilities	**€m**	**€m**	**€m**	€m
Loans and advances to customers	**6,814**	9,992	**6,814**	9,992

	Group		Bank	
	2017	**2016**	**2017**	2016
Liabilities secured by charges on assets	**€m**	**€m**	**€m**	€m
Debt securities in issue[1]	**5,281**	9,107	**-**	-
Deposits by banks	**341**	28	**341**	28
	5,622	9,135	**341**	28

(1) At 31 December 2017 all of the debt securities in issue from the Group were held as assets by the Bank and consolidated in the Group accounts (2016: €7,731m).

During the financial year all of the mortgage backed securities issued by four securitisation vehicles were redeemed at par. These limited recourse entities were controlled by the Group and included in the consolidated financial statements on that basis. At 31 December 2016 the value of the mortgage backed securities issued by these four securitisation vehicles was €3,493m, of which €2,118m was held by the Bank and consolidated in the Group accounts.

At the balance sheet date the Bank had pledged €236m (2016: €236m) of the debt securities to RBS plc as collateral against intraday SEPA payments which RBS plc processes on behalf of the Bank. A further €20m (2016: €60m) of debt securities were pledged as collateral to UBPS and €17m (2016: €nil) of debt securities were pledged as collateral to the trustees of First Active Pension Scheme under contingent asset arrangements put in place to cover the Risk Reserve requirements arising under the Minimum Funding Standard framework.

Securitisations and other asset transfers

The Group undertakes securitisations to fund specific portfolios of assets. In a securitisation, assets, or interests in a pool of assets, are transferred generally to a special purpose entity (SPE) which then issues liabilities to third party investors. SPEs are vehicles established for a specific, limited purpose, usually do not carry out a business or trade and typically have no employees. They take a variety of legal forms - trusts, partnerships and companies - and fulfil many different functions.

It is primarily the extent of risks and rewards assumed that determines whether these entities are consolidated in the Group's financial statements.

23. Collateral and securitisations (continued)

Securitisations and other asset transfers (continued)

The following table sets out the asset categories together with the carrying amounts of the assets and associated liabilities for those securitisations where substantially all the risks and rewards of the asset have been retained by the Group and continue to be presented in its balance sheet.

	Group			
	2017		2016	
	Assets	**Liabilities**	Assets	Liabilities
	€m	**€m**	€m	€m
Residential mortgages	**6,814**	**-**	9,992	1,377

	Bank			
	2017		2016	
	Assets	**Liabilities**	Assets	Liabilities
	€m	**€m**	€m	€m
Residential mortgages	**6,814**	**-**	9,992	-

The Bank's securitised mortgages reduced during the financial year as a result of the redemption of the debt securities of four securitisation vehicles.

24. Risk management

Risk overview
The management of risk is a fundamental activity performed throughout all of the Group’s operations. As such, it underpins the Group’s reputation, performance and future success.

Risk culture
A sound risk culture is essential to the realisation of the Group's ambition to be number one for customer service, trust and advocacy. The Group’s objective is to embed a risk culture that supports appropriate risk awareness, behaviours and judgements about risk-taking.

Employees at all levels are responsible for the management of risk. The Group requires employees to exhibit behaviours that support a sound risk culture where risk is part of the way its employees work and think. The behaviours supporting this risk culture are based strongly on tone from the Board and Executive Committee and those behaviours that support are acknowledgement, transparency, respect and responsiveness to risk. These behaviours are aligned to the Group’s values of ‘serving customers’, ‘working together’, ‘doing the right thing’ and ‘thinking long-term’.

Aligned to these values is Our Code. Our Code provides guidance on expected behaviours and sets out the standards of conduct that support the values. It explains how the values can effect and support decisions that are taken and describes the principles that must be followed.

Three lines of defence
The Group uses the three lines of defence model to articulate accountabilities and responsibilities for managing risk across the organisation. The three lines of defence model is adopted across the industry to support the embedding of effective risk management and is expressed through a set of principles as outlined below:

First line of defence – management and supervision
The first line of defence includes customer facing business units, Technology and Services, as well as support and control functions such as Human Resources, Communications & Marketing and Finance. Responsibilities include:
- Owning, managing and supervising, within a defined risk appetite, the risks which exist in business areas and support functions.
- Ensuring appropriate controls are in place to mitigate risk, balancing control, customer service and competitive advantage.
- Ensuring that the culture of the business supports balanced risk decisions and compliance with policy, laws and regulations.
- Ensuring the business has effective mechanisms for identifying, reporting and managing risk and controls.

24. Risk management (continued)

Three lines of defence (continued)

Second line of defence – oversight and control
The second line of defence includes Risk, Legal, and the financial control element of the Group's Finance function. Responsibilities include:

- Working with the businesses and functions to develop risk and control policies, limits and tools for the business to use in order to discharge its responsibilities.
- Overseeing and challenging the management of risks and controls.
- Leading the articulation, design and development of risk culture and appetite.
- Analysing the aggregate risk profile and ensuring that risks are being managed within risk appetite.
- Providing expert advice to the business on risk management.
- Providing senior executives with relevant management information and reports, and escalating concerns where appropriate.

Third line of defence – Internal Audit
Responsibilities include:

- Providing assurance to the Audit Committee that the main business risks have been identified and effective controls are in place to manage these risks.
- Engaging with management to provide perspectives, insights and challenge in order to influence the building of a sustainable bank.
- Providing independent assurance to the CBI on specific risks and control.

Risk appetite
Risk appetite defines the level and types of risk the Group is willing to accept, within risk capacity, in order to achieve its strategic objectives and business plans. Risk appetite is important because understanding and managing risks are core components of keeping the bank safe and secure. It ensures the Group strikes an optimal balance between building a sustainable business and creating long-term value for its customers and stakeholders. Risk capacity defines the maximum level of risk the Group can assume before breaching constraints determined by regulatory capital and liquidity needs, the operational environment, and from a conduct perspective. Articulating risk capacity is helpful in determining where risk appetite should be set, ensuring there is a buffer between internal risk appetite and the Group's ultimate capacity to absorb losses.

Risk appetite framework
The risk appetite framework bolsters effective risk management by promoting sound risk taking and ensuring emerging risk and risk taking activities are recognised, assessed, escalated and addressed in a timely manner.

The Board approves the risk appetite framework annually.

Strategic risks
Strategic risks are the foundations upon which the Group ensures it remains safe and sound while implementing its strategic business objectives. They are:

Risk type	How the risk arises
Capital adequacy risk	Capital adequacy risk is the risk of not being able to conduct business in base or stress conditions due to insufficient qualifying capital as well as the failure to assess, monitor, plan and manage capital adequacy requirements.
Liquidity and funding risk	Liquidity risk is the risk of being unable to meet financial obligations as and when they fall due. Funding risk is the risk of not maintaining a diversified, stable and cost-effective funding base.
Earnings volatility risk	Earnings volatility risk measures the volatility of earnings under stress of the planned periods relative to previous year profit. If the base plan shows a loss the Bank is outside of appetite.
Stakeholder confidence risk	Stakeholder confidence is a measure of how much our key stakeholders trust, respect and value the bank. It is the end result of the ability (or otherwise) of the bank to suitably manage the strategic and material risks which it is exposed to. It is expected that by achieving our strategic and financial plans and effectively managing risks within risk appetite we should attain our desired level of stakeholder confidence.

24. Risk management (continued)

Material risks
The Material Risk Assessment (MRA) is a key input into the Internal Capital Adequacy Assessment Process (ICAAP) and is used to substantiate risks that are material to the profitability and sustainability of the Bank. It acts as a key element of the Bank's overall risk management framework and allows the linkage of capital management between material risks, risk appetite and policy frameworks to be evidenced. As result of this exercise the Group identified the following level 1 risks as material to the bank in addition to the four strategic risks above.

- Business risk;
- Reputational risk;
- Conduct risk;
- Compliance risk;
- Operational risk;
- Pension risk;
- Credit risk; and
- Non-traded market risk.

All of the level 1 risks influence and impact on the strategic risks. For example, Operational Risk impacts all four strategic risks and therefore strategic and level 1 risks cannot be considered in isolation.

The Board sets risk appetite for strategic and material risks to help ensure the Group is well placed to meet its priorities and long-term targets, even under challenging economic conditions.

Further detail on the material level 1 risks and how they may arise is set out in the table below.

Risk type	How the risk arises
Business risk	Business risk arises as a result of the Bank's exposure to the macro-environment, to the competitive environment and to technological changes. In addition, internal factors such as volatility in sales volumes and input costs, and other operational risks such as the Group's ability to assess the business operating environment, or to execute its chosen strategy, contribute to business risk.
Reputational risk	Reputational risk can arise from the failure to meet the expectations of key stakeholders (customers, employees, investors, regulators, media and the general public) in relation to our performance, conduct and business profile.
Conduct and compliance risk	Conduct and compliance risk arises if the conduct of the Bank and its staff towards its customers leads to damage arising from breaches of regulatory requirements or customer expectations or if the Bank fails to comply with laws, regulations, rules, related self-regulatory organisation standards, and codes of conduct applicable to its regulated activities.
Operational risk	Operational risk arises from a failure to manage operations, transactions and assets appropriately. It may arise from human error, an inability to deliver change on time or adequately, or the unavailability of technology services or the loss of customer data. Fraud and theft are sources of operational risk, as is the impact of natural and man-made disasters. It may also arise from a failure to take appropriate measures to protect assets or take account of changes in law.
Pension risk	Pension risk arises due to contractual or other liabilities to or with respect to pension schemes, whether established for its employees or those of a related company or otherwise. It also means the risk that the Bank will make payments or other contributions to or with respect to a pension scheme because of a moral obligation or because the Bank considers that it needs to do so for some other reason.
Credit risk	Credit risk arises from lending and available-for-sale debt securities. Counterparty credit risk results from derivatives and securities financing transaction activities.
Market risk	The majority of the Group's market risk relates to non-traded market risk exposure from retail and commercial banking activities from assets and liabilities that are not classified as held-for-trading or the risk to income, which arises from changes in market prices such as interest rates, foreign exchange rates, and equity prices, or from changes in managed rates.

24. Risk management (continued)

Risk appetite statements
Risk appetite is communicated across the Group through risk appetite statements. Each statement provides clarity on the scale and type of activities permitted, in a manner that is easily conveyed to staff. Risk appetite statements consist of quantitative and qualitative statements of appetite supported by risk limits and triggers that operate as a defence against excessive risk-taking.

The purpose of risk appetite statements is to strengthen understanding of acceptable levels of risk. The risk appetite statements are established at a Group-wide level for strategic risks and material risks.

The annual process of establishing risk appetite statements is completed alongside the business and financial planning process to ensure risk appetite remains appropriate given the levels of risk expected over the planning horizon. Risk appetite statements are reviewed on a regular basis during the year and proposed amendments to existing statements or new statements proposed are approved by Board as necessary. The effective communication of risk appetite is essential in embedding appropriate risk-taking into the Group's culture.

The Group frequently reviews its risk profile to ensure it remains within risk appetite and that management focus is brought to bear on all material risks and emerging risk issues. The Group has effective processes in place to report against risk appetite to the Board and senior management.

Capital adequacy risk
Capital consists of financial resources and instruments issued that are available to the Bank and that have a degree of permanency and are capable of absorbing losses. A number of strict conditions set by regulators must be satisfied to be eligible to count as capital.

Capital adequacy risk is the risk of being unable to conduct business in base or stress conditions due to insufficient qualifying capital as well as the failure to assess, monitor, plan and manage capital adequacy requirements.

Capital management is the process by which the Bank manages its capital risk and is a key focus of its risk management activities.

Constituents of capital
The determination of what instruments and financial resources are eligible to be counted as capital is laid down by applicable regulation.

Capital is categorised by applicable regulation under two tiers (1 and 2) according to the ability to absorb losses, degree of permanency and the ranking of absorbing losses. There are three broad categories of capital across these two tiers:

- **Common Equity Tier 1 (CET1) capital**. CET1 capital must be perpetual and capable of unrestricted and immediate use to cover risks or losses as soon as these occur. This includes ordinary shares issued and retained earnings. CET1 capital absorbs losses before other types of capital and any loss absorbing instruments.
- **Additional Tier 1 (AT1) capital**. AT1 capital is the second form of loss absorbing capital and must be capable of absorbing losses on a going concern basis. These instruments are either written down or converted into CET1 capital when a pre-specified CET1 ratio is reached. Coupons on AT1 issuances are discretionary and may be cancelled at the discretion of the issuer at any time. AT1 capital must have a minimum maturity of five years.
- **Tier 2 capital**. Tier 2 capital is the Bank's supplementary capital and provides loss absorption on a gone concern basis. Tier 2 capital absorbs losses after Tier 1 capital. It typically consists of subordinated debt securities with a minimum maturity of five years.

In addition to capital, other specific loss absorbing instruments may be used to cover certain gone concern capital requirements which, in the EU, is referred to as minimum requirement for own funds and eligible liabilities (MREL).

The Bank does not currently hold any AT1 or MREL instruments but these are kept under consideration for capital planning purposes.

Capital adequacy ratios
The Bank has to hold a minimum amount and quality of capital to satisfy regulatory capital adequacy requirements.

Risk-weighted assets
Capital adequacy ratios compare the amount of capital held to risk-weighted assets (RWAs). RWAs are a measure of the Bank's assets and off-balance sheet positions that capture both the size and risks inherent in those positions.

24. Risk management (continued)

Risk-weighted assets (continued)

For regulatory purposes, RWAs are grouped into four categories:

Risk	Description
Credit	Risk of loss from a borrower failing to repay amounts due by the due date.
Counterparty credit	Risk of loss from a counterparty not meeting its contractual obligations. Also included is the risk of loss from changes in the fair value of derivative instruments.
Market	Risk of loss arising from fluctuations in market prices.
Operational	Risk of loss from inadequate or failed internal processes, people and systems or from external events.

Minimum percentage
Regulation defines a minimum percentage of capital compared to RWAs. There are two broad categories of capital requirements:

Category	Description
Minimum capital adequacy ratio	Represents the minimum amount of capital that all banks must hold at all times.
Capital buffers	Capital required to be held by banks that may be used in periods of stress.

The Group may be required to hold capital over and above the minimum requirements under the Pillar 2 framework. Pillar 2 looks at capital that may need to be held by the Bank against risks that are not fully captured or not captured under minimum requirements and risks across a forward-looking planning horizon.

Leverage ratios
The Bank has to hold a minimum amount and quality of capital to satisfy the leverage ratio regulatory requirements. Unlike capital adequacy ratios, leverage ratio requirements do not consider the riskiness of the Bank's positions.

The leverage exposure is broadly aligned to the accounting value of the Bank's on and off-balance sheet exposures but subject to certain adjustments for trading positions, repurchase agreements and off-balance sheet exposures.

In common with capital adequacy ratios, the leverage ratio requirement for the Bank consists of a minimum requirement and a leverage ratio buffer.

Capital management
Capital management is the process by which the Bank ensures that it has sufficient capital and other loss absorbing instruments to operate effectively including meeting minimum regulatory requirements, operating within the Board approved Group risk appetite, maintaining its credit rating and supporting its strategic goals.

In the management of capital resources, the Bank is governed by the UBIDAC and RBS policies which are to maintain a strong capital base, to expand it as appropriate and to utilise it efficiently throughout its activities to optimise the return to shareholders while maintaining a prudent relationship between the capital base and the underlying risks of the business.

In carrying out these policies the Bank has regard to and has complied with the capital supervisory requirements of the ECB and CBI throughout the financial year.

Capital management is critical in supporting the Bank's business and is enacted through a Group-wide end to end framework. The key elements of the Group capital management approach are set out below.

Risk appetite
Capital risk appetite is set by the Board, reflecting the Group's strategic objectives, current and future prudential regulatory requirements and market expectations.

It is expressed as a set of target ratios for CET1 total capital and leverage under both normal and stress financial conditions. Performance against risk appetite is regularly monitored.

24. Risk management – capital adequacy risk (continued)

Capital management (continued)

Capital planning
Capital planning is integrated into the Group's wider annual budgeting process and is one of the tools that the Group uses to monitor and manage the risk of excessive leverage.

Stress testing
Stress testing is a key risk management tool used by the Group, covering the Bank and its businesses, and is a fundamental component of the Group's approach to capital management.

Stress testing is used to quantify, evaluate and understand the potential impact on the financial strength of the Group, including its capital position, given specified changes to risk factors. Stress testing includes:

- *Scenario testing:* to examine the impact of a hypothetical future state of the world to define changes in risk factors affecting the Group; and
- *Sensitivity testing:* to examine the impact of an incremental change to one or more risk factors.

Specific areas that involve capital management include:
- **Strategic financial and capital planning**: through assessing the impact of sensitivities and scenarios on the capital plan and capital ratios;
- **Risk appetite**: through gaining a better understanding of the drivers of and the underlying risks associated with risk appetite;
- **Risk identification**: through a better understanding of the risks that could potentially impact the Group's financial strength and capital position; and
- **Risk mitigation**: through identifying actions that can be taken to mitigate risks or could be taken in the event of adverse changes to the business or economic environment. Risk mitigation is substantially supplemented through the Group's recovery plan.

Internal assessment of capital adequacy
The ICAAP is an annual internal assessment conducted by the Group to assess its material risks and evaluate how much capital is required to cover these risks. The ICAAP is approved by the Board and submitted to regulators.

The ICAAP consists of a point in time capital assessment of the Group's exposures and risks at the financial year end and a forward looking stress capital assessment.

The ICAAP is used by the Group to form a view of capital adequacy separately to the regulatory minimum requirements. The ICAAP is used by the CBI and ECB to make an assessment of bank-specific capital requirements through the Supervisory Review and Evaluation Process (SREP) framework.

Governance
Capital management is subject to substantial review and governance across the Group including capital management policies that are approved by ALCO and/or Board Risk Committee. The Board approves the Group's capital plans.

Recovery and resolution planning
The Group maintains an internal UBIDAC Recovery Framework (URF) that sets out credible recovery options that could be implemented in the event of a stress to restore its business to a stable and sustainable condition. Elements of this URF are subsequently incorporated into the RBS Group Recovery Plan.

The URF sets out a range of triggers that activate the implementation of the framework and sets out the operational plan for its implementation. The URF is a key component of the overall risk management of the Group and is updated and approved by the Board quarterly.

The Bank of England is the Resolution authority for RBSG, including the Group, under the single point of entry principle.

Liquidity and funding risk

Definition
Liquidity and funding risk is the risk that the Group is unable to meet its financial obligations, including financing wholesale maturities or customer deposit withdrawals, as and when they fall due.

24. Risk management – liquidity and funding risk (continued)

Sources of liquidity and funding
Liquidity and funding risk arises through the maturity transformation role that banks perform, lending long-term but obtaining funding predominantly through short-term liabilities such as customer deposits. It is dependent on Group-specific factors such as maturity profile, composition of sources and uses of funding, the quality and size of the liquidity portfolio as well as broader market factors, such as wholesale market conditions alongside depositor and investor behaviour.

The Group's primary funding sources are as follows:

Type	Description
Customer deposits	Retail and Corporate deposits.
Wholesale markets	Short-term (less than 1 year) unsecured money markets and secured repo market funding.
Term debt	Issuance of long-term (more than 1 year) unsecured and secured debt securities.

The Group may access various funding facilities offered by central banks from time to time. The use of such facilities can be both part of a wider strategic objective to support initiatives to help stimulate economic growth or as part of the broader liquidity management and funding strategy. Usage and repayment of available central bank facilities will fit within the overall liquidity risk appetite and concentration limits.

Policy, risk appetite and governance
The key elements of the Group's liquidity and funding framework are as follows:

Type	Description
Risk appetite	Meeting regulatory and set internal risk limits for liquidity and funding.
Policies	Managing liquidity and funding across the Group.
Governance	Management oversight and three lines of defence.

Internal liquidity and funding policies are designed to ensure that the Group:

- *Has a clearly stated liquidity and funding risk tolerance*: the appetite for liquidity risk is set by the Board as a percentage of Regulatory Liquidity Coverage. The Board also sets the appetite for funding risk to ensure that stable sources of funding are used to fund the Group's core assets. The Group monitors its liquidity and funding positions against these risk tolerances on a daily basis. In setting risk limits the Board considers the nature of the Group's activities, overall risk appetite, market best practice and regulatory compliance.
- *Has in place strategies, policies and practices to ensure that the Group maintains sufficient liquidity*: the risk management framework determines the sources of liquidity risks and the steps that can be taken when these risks exceed certain actively monitored limits. These actions include when and how to use the liquid asset portfolio, and what other adjustments to the balance sheet should be undertaken to manage these risks within the Group's risk appetite.
- *Incorporates liquidity costs, benefits and risks in product pricing and performance management*: the Group uses internal funds transfer pricing to ensure that these costs are reflected in the measurement of business performance and to correctly incentivise businesses to source the most appropriate mix of funding.

The liquidity and funding risk tolerance forms part of the Group's risk appetite statement, which is overseen by the Board Risk Committee and then approved by the Board. The risk appetite statement defines key metrics, risk trigger levels and capacity for liquidity and funding management within the Group. The Asset and Liability Management Committee (ALCO), oversees the implementation of liquidity and funding management across the Group in accordance with set risk appetite.

24. Risk management - liquidity and funding risk (continued)

Regulatory oversight
The Group operates under the financial supervision of the ECB, with the key regulatory metrics being:

Ratio	Exposure type	Description
Liquidity coverage ratio	Liquidity profile	Coverage of 30 day net cash outflows in stress.
Net stable funding ratio	Structural funding profile	Required and available stable funding sources less than and greater than 1 year timeline.
CBI Maturity Mismatch	Liquidity and funding profile	Maturity mismatch approach for cash flows by time band, with consideration of liquid assets held. This was discontinued on 1 January 2018 in accordance with Article 412(5) CRR, following full introduction of 100% LCR requirement.

Liquidity risk regulation for the Group is driven by the quantitative and qualitative requirements of the CBI with financial supervision now joint with the ECB under the Single Supervisory Mechanism (SSM).

Activity	Description
ILAAP	An annual process undertaken in compliance with regulatory guidance to formalise the Group's approach to understanding its liquidity risk profile and the processes and systems it needs to have in place to assess, quantify and monitor these risks.
SREP	One of the pillars of the SSM's SREP process is to review liquidity and funding of the Group. This involves a comprehensive review of the Group ILAAP, liquidity policies and risk management framework.

Measurement, monitoring and contingency planning
A suite of tools are used to monitor, limit and stress test the liquidity and funding risks within the balance sheet. The limits control the amount and composition of funding sources, asset and liability mismatches and funding concentrations, in addition to the level of liquidity risk.

Liquidity risks are reviewed daily, with performance reported to ALCO at least monthly. Any breach of internal metric limits will set in motion a series of actions and escalations outlined under the Group recovery plan. The plan sets out credible recovery options that could be implemented in the event of severe stress to restore the business to a stable and sustainable position, focussing on addressing the Bank's capital and liquidity position.

Stress testing
The Group carries out a regular assessment of net stressed liquidity outflows. The Group considers a range of severe but plausible stress scenarios on cash flows, liquidity resources, profitability, solvency, asset encumbrance and survival horizon.

Type	Description
Idiosyncratic scenario	The market perceives the Group to be suffering from a severe stress event which results in an immediate assumption of increased credit risk or concerns over solvency.
Market-wide scenario	A market stress event affecting all participants in a market through contagion, counterparty failure and other market risks. The Group is impacted under this scenario but no more severely than any other participant with equivalent exposure.
Combined scenario	This scenario models the combined impact of an idiosyncratic and market stress occurring at once. The combined scenario reflects the contingency that a severe name-specific event occurs at the Group in conjunction with a broader market stress, causing wider damage to the market and financial sector and severely impacting funding markets and assets.

The Group uses the most severe of the three outcomes above to set the internal stress testing view. The results of this enable the bank to set its internal liquidity risk appetite to complement the regulatory LCR requirement.

As part of the ILAAP, the Group maintains an ILAAP-specific scenario of a cyber attack in conjunction with an extreme Brexit outcome, in addition to the other internal liquidity stress tests.

24. Risk management - liquidity and funding risk (continued)

Liquidity portfolio
The Group's balance sheet composition is a function of the broad array of product offerings and diverse markets served. The structural composition of the balance sheet is enhanced as needed through active management of both asset and liability portfolios. The objective of these activities is to optimise liquidity transformation in normal business environments, while ensuring adequate coverage of all cash requirements under extreme stress conditions.

The Group also accesses professional markets funding by way of public and private debt issuances on an unsecured and secured basis. These debt issuance programmes are spread across maturities, to appeal to a broad range of investor types and preferences around the world. This market-based funding supplements the Group's structural liquidity needs and, in some cases, achieves certain capital objectives.

Contractual maturity
The following tables analyse the contractual undiscounted cash flows receivable and payable including future receipts and payments of interest on the balance sheet items by contractual maturity. The balances in the tables below do not agree directly to the Group or Bank balance sheets, as the tables include all cash flows relating to principal and future coupon payments presented on an undiscounted basis.

	Group						
	0–3 months	**3–12 months**	**1–3 years**	**3–5 years**	**5–10 years**	**10–20 years**	**>20 years**
2017	**€m**	**€m**	**€m**	**€m**	**€m**	**£m**	**€m**
Assets by contractual maturity							
Cash and balances at central banks	322	-	-	-	-	-	-
Loans and advances to banks	4,892	-	-	-	1	-	-
Debt securities	296	1,021	728	-	-	-	-
Total maturing assets	5,510	1,021	728	-	1		-
Loans and advances to customers	1,414	1,772	4,179	3,931	6,099	6,929	1,915
Total assets	**6,924**	**2,793**	**4,907**	**3,931**	**6,100**	**6,929**	**1,915**
Liabilities by contractual maturity							
Deposits by banks	480	1,504	502	-	2	-	-
Subordinated liabilities	-	6	10	540	25	98	2
Total maturing liabilities	480	1,510	512	540	27	98	2
Customer accounts	16,455	2,228	1,064	76	-	-	-
Derivatives held for hedging	-	1	2	-	-	-	-
Total liabilities	**16,935**	**3,739**	**1,578**	**616**	**27**	**98**	**2**
Maturity gap	**(10,011)**	**(946)**	**3,329**	**3,315**	**6,073**	**6,831**	**1,913**
Cumulative maturity gap	**(10,011)**	**(10,957)**	**(7,628)**	**(4,313)**	**1,760**	**8,591**	**10,504**
Guarantees and commitments notional amount							
Guarantees [1]	154	-	-	-	-	-	-
Commitments [2]	3,516	-	-	-	-	-	-
	3,670	-	-	-	-	-	-

For notes relating to this table, refer to page 78.

24. Risk management - liquidity and funding risk (continued)

Contractual maturity (continued)

	Group						
	0–3 months	3–12 months	1–3 years	3–5 years	5–10 years	10–20 years	>20 years
2016	€m	€m	€m	€m	€m	€m	€m
Assets by contractual maturity							
Cash and balances at central banks	290	-	-	-	-	-	-
Loans and advances to banks	4,545	1	-	-	76	-	-
Debt securities	428	974	953	-	-	-	-
Total maturing assets	5,263	975	953	-	76	-	-
Loans and advances to customers	1,583	1,582	3,793	4,133	6,017	6,750	2,027
Total assets	6,846	2,557	4,746	4,133	6,093	6,750	2,027
Liabilities by contractual maturity							
Deposits by banks	133	8	1,506	1	-	-	-
Debt securities in issue	24	69	167	145	284	343	389
Subordinated liabilities	-	8	55	50	566	106	35
Total maturing liabilities	157	85	1,728	196	850	449	424
Customer accounts	15,178	2,673	1,036	78	-	-	-
Total liabilities	15,335	2,758	2,764	274	850	449	424
Maturity gap	(8,489)	(201)	1,982	3,859	5,243	6,301	1,603
Cumulative maturity gap	(8,489)	(8,690)	(6,708)	(2,849)	2,394	8,695	10,298
Guarantees and commitments notional amount							
Guarantees [1]	179	-	-	-	-	-	-
Commitments [2]	3,510	-	-	-	-	-	-
	3,689	-	-	-	-	-	-

For notes relating to this table, refer to page 78.

24. Risk management – liquidity and funding risk (continued)

Contractual maturity (continued)

	Bank						
2017	**0–3 months €m**	**3–12 months €m**	**1–3 years €m**	**3–5 years €m**	**5–10 years €m**	**10–20 years €m**	**>20 years €m**
Assets by contractual maturity							
Cash and balances at central banks	322	-	-	-	-	-	-
Loans and advances to banks	4,892	-	-	-	1	-	-
Debt securities	5,578	1,021	728	-	-	-	-
Total maturing assets	10,792	1,021	728	-	1	-	-
Loans and advances to customers	1,829	1,772	4,179	3,931	6,099	6,929	1,915
Total assets	**12,621**	**2,793**	**4,907**	**3,931**	**6,100**	**6,929**	**1,915**
Liabilities by contractual maturity							
Deposits by banks	479	1,504	502	-	2	-	-
Subordinated liabilities	-	6	10	540	25	98	2
Total maturing liabilities	479	1,510	512	540	27	98	2
Customer accounts	22,160	2,228	1,064	76	-	-	-
Derivatives held for hedging	-	1	2	-	-	-	-
Total liabilities	**22,639**	**3,739**	**1,578**	**616**	**27**	**98**	**2**
Maturity gap	**(10,018)**	**(946)**	**3,329**	**3,315**	**6,073**	**6,831**	**1,913**
Cumulative maturity gap	**(10,018)**	**(10,964)**	**(7,635)**	**(4,320)**	**1,753**	**8,584**	**10,497**
Guarantees and commitments notional amount							
Guarantees [1]	**154**	-	-	-	-	-	-
Commitments [2]	**3,516**	-	-	-	-	-	-
	3,670	**-**	**-**	**-**	**-**	**-**	**-**

For notes relating to this table, refer to page 78.

24. Risk management – liquidity and funding risk (continued)

Contractual maturity (continued)

	Bank						
2016	0–3 months €m	3–12 months €m	1–3 years €m	3–5 years €m	5–10 years €m	10–20 years €m	>20 years €m
Assets by contractual maturity							
Cash and balances at central banks	290	-	-	-	-	-	-
Loans and advances to banks	4,226	1	-	-	76	-	-
Debt securities	8,158	974	953	-	-	-	-
Total maturing assets	12,674	975	953	-	76	-	-
Loans and advances to customers	2,067	1,582	3,793	4,133	6,017	6,750	2,027
Total assets	14,741	2,557	4,746	4,133	6,093	6,750	2,027
Liabilities by contractual maturity							
Deposits by banks	133	8	1,506	1	-	-	-
Subordinated liabilities	-	8	55	50	566	106	35
Total maturing liabilities	133	16	1,561	51	566	106	35
Customer accounts	24,773	2,673	1,036	78	-	-	-
Total liabilities	24,906	2,689	2,597	129	566	106	35
Maturity gap	(10,165)	(132)	2,149	4,004	5,527	6,644	1,992
Cumulative maturity gap	(10,165)	(10,297)	(8,148)	(4,144)	1,383	8,027	10,019
Guarantees and commitments notional amount							
Guarantees [1]	179	-	-	-	-	-	-
Commitments [2]	3,510	-	-	-	-	-	-
	3,689	-	-	-	-	-	-

(1) The Bank is only called upon to satisfy a guarantee when the guaranteed party fails to meet its obligations. The Bank expects most guarantees it provides to expire unused.
(2) The Bank has given commitments to provide funds to customers under undrawn formal facilities, credit lines and other commitments to lend subject to certain conditions being met by the counterparty. The Bank does not exp8ect all the facilities to be drawn, and some may lapse before drawdown.

24. Risk management – liquidity and funding risk (continued)

Contractual maturity (continued)

The contractual maturity of balance sheet assets and liabilities reflects the maturity transformation role banks perform. In practice, the behavioural profiles of many liabilities exhibit greater stability and longer maturity than the contractual maturity. This is particularly true of many types of retail and corporate deposits which, despite being repayable on demand or at short notice, have demonstrated very stable characteristics even in periods of acute stress. In analysis to assess and manage asset and liability maturity gaps the Group determines the expected customer behaviour through qualitative and quantitative techniques, incorporating observed customer behaviours over long periods of time. Procedures for determining expected behaviour are subject to regulatory and internal requirements and are stressed according to these requirements. The policy and key inputs for managing maturity and behavioural analysis are subject to governance through ALCO.

Financial assets have been reflected in the time band of the latest date on which they could be repaid unless earlier repayment can be demanded by the Group; financial liabilities are included at the earliest date on which the counterparty can require repayment regardless of whether or not such early repayment results in a penalty.

If the repayment of a financial asset or liability is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the asset is included in the latest date on which it can repay regardless of early repayment whereas the liability is included at the earliest possible date that the conditions could be fulfilled without considering the probability of the conditions being met.

Other contractual cash obligations

	Group and Bank						
2017	**0–3 months €m**	**3–12 months €m**	**1–3 years €m**	**3–5 years €m**	**5–10 years €m**	**10–20 years €m**	**>20 years €m**
Operating leases	**3**	**9**	**19**	**12**	**18**	**10**	**-**
Contractual obligations to purchase goods or services	**1**	**2**	**1**	**-**	**-**	**-**	**-**
	4	**11**	**20**	**12**	**18**	**10**	**-**

	Group and Bank						
2016	0–3 months €m	3–12 months €m	1–3 years €m	3–5 years €m	5–10 years €m	10–20 years €m	>20 years €m
Operating leases	4	10	20	14	16	5	-
Contractual obligations to purchase goods or services	-	2	3	-	-	-	-
	4	12	23	14	16	5	-

Business risk

Definition
Business risk is the risk that the Group makes inappropriate business or strategic choices or that the Group is not able to execute its chosen strategy in line with its budget. The risk is that the Group does not deliver its strategic plan's budgeted performance which could lead to a deterioration in stakeholder trust and confidence or to a breach of regulatory thresholds.

Sources of risk
Business risk arises as a result of the Bank's exposure to the macro-environment, to the competitive environment, and to technological changes. Current macro issues that give rise to business risk include Brexit, cyber threats, corporate structure reform and political and economic uncertainty. In addition, internal factors such as volatility in sales volumes, and input costs, and other operational risks such as the Group's ability to assess the business operating environment, or to execute its chosen strategy, contribute to business risk.

24. Risk management - business risk (continued)

Governance
The Board has ultimate responsibility for business risk and for approving strategic plans, initiatives and changes to strategic direction. The Group's strategic planning process is managed by the Strategic Finance department. The Risk and Finance functions are key contributors to strategic planning. As part of the process, each customer business develops a strategic plan within a process set by the Group's Executive Committee. The strategic plans are consolidated at the Group-wide level, and reviewed and assessed against risk appetite by the Chief Executive, the Chief Financial Officer and the Director of Risk before review, challenge and ultimately approval by the Board.

Risk assessment, controls and assurance
Business risk is directly managed and controlled through the Group's strategic planning, budgeting and new product development processes, in which the following elements are incorporated:

- Evaluation of the macroeconomic environment;
- Industry analysis;
- Competitor analysis, across geography, product, and customer;
- Customer behaviour analysis (understanding customer segments, trends and behaviours);
- Impact of technological developments;
- Assessment of regulatory developments and changes; and
- Evaluation of the political environment.

Furthermore, business risk is controlled as a result of having a requirement for the Group and each business to incorporate the following elements in strategic plans:

- Organisational capabilities;
- Organisational resources;
- Organisational commitment; and
- Requirements of stakeholders, including customers, regulators, employees, and investors.

Risk appetite
The Group has limited appetite to make inappropriate business or strategic choices or to deliver a financial performance that is materially worse than its chosen strategic business plan.

Risk identification and assessment
Estimated revenue, costs and capital, including the potential range of outcomes, are key considerations in the design of any new product or in any new investment decision.

Risk mitigation
The Group operates a monthly rolling forecasting process to identify projected changes in, or risks to, key financial metrics, and ensures appropriate actions are taken.

Key strategies are reviewed and approved by the Board. These reviews are intended to maximise the capture of market and customer insight while providing independent scrutiny and challenge. Strategic plans contain analysis of current and expected operating conditions, current and targeted competitive and market positioning, key strategic initiatives, financial and customer targets and milestones, and upside and downside risks.

A full sensitivity analysis of the consolidated strategic plan is undertaken at the end of the strategic and financial planning process to assess the robustness of the plan and compliance with strategic risk objectives under a variety of stressed conditions. Following consideration of an opportunity the Group may decide not to pursue the opportunity as a result of a perceived strategic risk.

The Group also undertakes strategic reviews to decide on how to react to specific developments.

Reputational risk

Definition
Reputational risk is the risk to the Bank's public image from a failure to meet stakeholders' expectations in relation to performance, conduct or business profile. Stakeholders include customers, investors, employees, suppliers, government, regulators, special interest and consumer groups, media and the general public.

Sources of risk
Reputational risk can arise from the conduct of employees; activities of customers and the sectors and countries in which they operate; provision of products and transactions; as well as operations and infrastructure.

24. Risk management - reputational risk (continued)

Governance
The Group has a Reputational Risk Policy which sets out controls to manage the risk. A Reputational Risk Forum (RRF), under delegated authority from the Group's Executive Risk Committee, acts as a central forum to review customer transactions, themes or issues which have material reputational implications, escalated to it by first line of defence business areas. The forum also reviews reputational risk arising from environmental, social and ethical risk positions, for example, in the defence and gambling sectors. Cases which have material reputational risk implications for the wider RBS Group are escalated to the RBS Group RRF.

Risk appetite
The Group manages and articulates its appetite for reputational risk through the implementation of a qualitative reputational risk appetite statement. The Group has zero tolerance for avoidable reputational risks or damage. The Group relies on due consideration of its reputation in its decision making. As a minimum this should include using the Yes Check. The Group has no appetite for a lack of escalation of material reputational risks. Escalation and subsequent debate must be timely and holistic and involve all relevant stakeholders. The Group recognises that unforeseen outcomes occur from time to time.

Risk mitigation
Reputational risk is mitigated through clear escalation responsibilities of all staff through their business line, should they identify potential reputational risk impact, with the most material cases being submitted to the RRF. Referrals are recorded in a Reputational Risk Register.

Early identification and effective escalation are essential to the successful mitigation of reputational risk. Lessons learned from discussions at RRF meetings will improve the way cases and issues are debated and decisions made.

The most material threats to the Group’s reputation continued to originate from historical and more recent conduct issues.

Conduct and compliance risk

Definition
Conduct risk is the risk that the behaviour of the Group and its staff towards customers, or in the markets in which it operates, leads to unfair or inappropriate customer outcomes and results in reputational damage, financial loss or both. The damage or loss may be the result of a failure to comply with (or adequately plan for changes to) relevant laws, regulations, or major industry standards, or of failing to meet customers’ or regulators’ expectations.

Compliance risk, which includes Prudential risk and policy requirements, is the risk that the Bank fails to comply with laws, regulations, rules, related self-regulatory organisation standards, policies and codes of conduct applicable to regulated activities.

Sources of risk
Conduct risk exists across all areas of the Group and stages of the Group’s relationships with its customers, from the development of its business strategies to post-sales processes. The activities through which conduct risk may arise are varied and include product design, marketing and sales, complaint handling, staff training, and handling of confidential insider information. Conduct risk also arises if the Group does not take effective action to prevent fraud, bribery and money laundering.

In addition to the above, compliance risk, which covers all policy and Prudential requirements, arises if the Bank fails to comply with laws, regulations, rules, related self-regulatory organisation standards, policies and codes of conduct applicable to its regulated activities. Further details on Prudential risk are disclosed in the capital adequacy risk and liquidity and funding risk sections.

Governance
The Board is responsible for defining appropriate standards of conduct and compliance and driving adherence to them, designing the framework for managing these risks, and overseeing remediation activity. The Board and its senior committees receive updates on conduct and compliance risk exposures and action plans through regular reporting.

Controls and assurance
Under the Policy framework the Group has policies designed to meet Group requirements. The policies ensure the Group meets legislative and regulatory obligations, and provide the necessary clarity to staff on their conduct and compliance obligations.

Corporate Governance and Regulatory Affairs separately oversee interactions with regulators, including regulatory approvals for individuals in pre-approved controlled function roles.

24. Risk management - conduct and compliance risk (continued)

Controls and assurance (continued)
Assurance and monitoring activities are essential to measure the extent to which the Group manages its delivery of specific customer outcomes. Risk assessments are used to identify material conduct risks and implement key controls across all business areas. Key controls are identified in policies and these should be reflected in each risk assessment. The risk assessment process is designed to confirm that risks are effectively managed and prioritised, as well as to ensure controls are tested. Bi-annual assessments of policy compliance are completed by each policy owner and approved by the policy sponsor.

Scenario analysis is used to assess the impact of extreme but plausible conduct and compliance risks including financial crime. The scenarios assess the risks that could significantly affect the Group's financial performance or reputation and are an important component in the operational risk framework and capital model.

Risk appetite
The conduct risk appetite framework and the Conduct Performance Assessment, which forms part of it, facilitates a consistent approach across the Group for assessing conduct risk. The Bank has no appetite for not fulfilling its required obligations as per regulatory requirements.

Risk monitoring and measurement
Management reports on the most material matters to the appropriate committees, including Board Risk Committee, Audit Committee and Board. A compliance report is presented to Board Risk Committee and Board on a quarterly basis and where appropriate, compliance breaches are escalated through the Group Notifiable Event Process.

The Audit Committee is provided with a whistleblowing report on a bi-annual basis. It details cases by internal reporting categories based on the definition of whistleblowing, which is contained within the Group's Speak Up policy.

The Group continues to work with each business to enhance the management information linked to their risk appetite statements. This is required to help ensure appropriate customer outcomes are delivered and that management information is compliant with the Basel Committee on Banking Supervision's principles for effective risk data aggregation and risk reporting.

Risk mitigation
The Group operates a process whereby information is communicated to customer-facing businesses and functions about regulatory developments and discussions with regulators. This helps identify and execute any required mitigating changes to strategy or to business models.

Early identification and effective management of changes in legislation and regulation are critical to the successful mitigation of conduct risk. The effects of all changes are managed to ensure timely compliance readiness.

Operational risk

Definition
Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or external events. It arises from day-to-day operations and is relevant to every aspect of the business.

Operational risk may directly affect customers, lead to financial loss or damage the Group's reputation (for example, a major IT systems failure or fraudulent activity). There can also be a link between operational risk failures and conduct risk issues.

Sources of risk
Operational risk may arise from a failure to manage operations, systems, transactions and assets appropriately. This can take the form of human error, an inability to deliver change adequately or on time, the non-availability of technology services, or the loss of customer data. Fraud and theft are sources of operational risk, as is the impact of natural and man-made disasters. It can also arise from a failure to account for changes in law, regulations or taking appropriate measures to protect assets.

Risk governance
A strong Operational Risk management function is vital to support the Bank's ambition to serve its customers better. Improved management of operational risk against a defined appetite directly supports the strategic risk objective of improving stakeholder confidence and is vital for stability and reputational integrity.

The Operational Risk function, part of the second line of defence, undertakes a leadership role and is tasked with delivering an operational risk management framework across the Bank.

24. Risk management - operational risk (continued)

Risk governance (continued)
The Operational Risk function is responsible for the design, development, delivery and continuous improvement of the operational risk management framework through the Operational Risk Handbook. The Operational Risk policy is incorporated into the Bank policy framework and the Operational Risk Handbook provides direction for the consistent identification, assessment, management, monitoring and reporting of operational risk. Through a network of oversight teams, the function seeks to ensure the integrity of the framework, and manages overall operational risk profile against risk appetite.

Risk assessment, controls and assurance
The Control Environment Certification (CEC) process is a half-yearly self-assessment by the CEO. It gives an assessment on the adequacy and effectiveness of the internal control environment in a consistent and comparable manner, highlighting areas where targeted effort is needed to meet the standards required in order to create a safer and more secure bank for customers. It covers material risks and the key controls that underpin them, including financial, operational and compliance controls, as well as the supporting risk management frameworks.

The CEC outcomes, including forward-looking assessments for the next two half-yearly cycles and the progress made to improve the control environment, are reported to the Board, the Audit Committee and the Board Risk Committee. They are also shared with external auditors.

The CEC process helps to ensure compliance with the Bank Policy Framework.

Assurance and monitoring activities are essential to measure the extent to which the Bank manages its delivery of specific customer outcomes. Risk assessments are used to identify material risks and implement key controls across all business areas. The risk assessment process is designed to confirm that risks are effectively managed and prioritised, as well as ensure controls are tested.

Scenario analysis is used to assess the impact of extreme but plausible operational risks. It provides a forward-looking basis for evaluating and managing operational risk exposures. The scenarios assess the risks that could significantly affect the banks financial performance, customers or reputation and are an important component in the operational risk framework and economic capital model.

Risk appetite
The operational risk appetite framework supports effective management of key operational risks. It expresses the level and types of operational risk the Bank is willing to accept in order to achieve its strategic objectives and business plans.

The Bank's operational risk appetite is expressed through a set of qualitative risk appetite statements and quantitative measures which are defined at a material risk driver level. Appetite covers the Bank's most material operational risks, defined by a materiality assessment, which considers past, current and future risk exposures. Appetite exposures for all material risks are regularly reported to the Executive Risk Committee and Board Risk Committee.

The aggregation of operational risk appetite drives measurement of how effective the Bank is managing its material risks across the core components of the operational risk management framework. It provides for an aggregate view of risk appetite, risk and control profile, loss event data management and control environment.

Above these sit the Bank-level operational risk appetite statement which encompasses the full range of operational risks. This drives the strategic risk measurement of stakeholder confidence and is reviewed annually by the Executive Risk Committee, Board Risk Committee and Board. The statement is supported by three simple measures: (i) the relationship between operational risk losses and the Bank's capital held; (ii) individual losses experienced across material risks; and (iii) the requirement for the material Bank-wide operational risks to be managed within risk appetite.

Risk identification and assessment
Across all business areas, risk and control assessments are used to identify and assess material risks and key controls. To support identification of risk concentrations, all risks and controls are mapped to the risk directory. Risk assessments are refreshed at least annually or triggered when a material change occurs to ensure they remain relevant and capture any emerging risks.

The process is designed to confirm that risks are effectively managed and prioritised in line with the stated risk appetite. Controls are tested at the appropriate frequency to verify that they remain fit-for-purpose and operate effectively.

24. Risk management - operational risk (continued)

Risk mitigation
Risks are mitigated through the application of key preventative and detective controls. This is an integral step in the risk assessment methodology, which determines residual risk exposure. Control owners are accountable for the design, execution, performance and maintenance of key controls.

These key controls are assessed for adequacy and tested for effectiveness annually. The control testing results are monitored and, where a material change in performance is identified, it results in a re-evaluation of the associated risk.

The Bank purchases insurance to provide the business with financial protection against specific losses and to comply with statutory or contractual requirements.

Risk monitoring
Monitoring and reporting are part of the Bank's operational risk management processes, which aim to ensure that risks are identified, considered by senior executives, and managed effectively. The most material operational risks and their position relative to risk appetite are regularly reviewed by the Executive Risk Committee, along with any emerging risks and the actions taken to mitigate them. These are also reported to the Board Risk Committee.

Risk measurement
The Bank uses the standardised approach to calculate its operational risk capital requirement. This is based upon multiplying three years' average historical gross income by coefficients set by the regulator based on type of income.

As part of the wider ICAAP an operational risk economic capital model is used. The model uses loss data and scenario analysis inputs from the operational risk framework, plus external loss data and certain other factors to provide a risk-sensitive view of the Bank's operational risk capital requirement.

Event and loss data management
The operational risk event and loss data management process ensures the Bank captures and records operational risk loss events that meet defined criteria. Loss data is used for regulatory and industry reporting and is included in the economic capital modelling when calculating regulatory capital for operational risk.

The most serious events are escalated in a simple, standardised process to all senior management, by way of a 'Notifiable Event Process'.

All losses and recoveries associated with an operational risk event are reported against their financial accounting date. A single event can result in multiple losses (or recoveries) that may take time to crystallise. Losses and recoveries with a financial accounting date in 2017 may relate to events that occurred, or were identified in, prior years.

Pension risk

Definition
Pension risk arises due to contractual or other liabilities to or with respect to pension schemes, whether established for its employees or those of a related company or otherwise. It also means the risk that the Bank will make payments or other contributions to or with respect to a pension scheme because of a moral obligation or because the Bank considers that it needs to do so for some other reason.

Sources of risk
The Group is exposed to risk from its defined benefit pension schemes to the extent that the assets of the schemes do not fully match the timing and amount of the schemes' liabilities. Pension scheme liabilities vary with changes to long-term interest rates, inflation, pensionable salaries and the longevity of scheme members as well as changes in legislation. Ultimate responsibility for the Group's pension schemes is separate from Group management. The Group is exposed to the risk that the market value of the schemes' assets, together with future returns and any additional future contributions could be considered insufficient to meet the liabilities as they fall due. In such circumstances, the Group could be obliged, or may choose, to make additional contributions to the schemes or be required to hold additional capital to mitigate such risk.

24. Risk management - pension risk (continued)

Sources of risk (continued)
The UBPS is the largest of the schemes and the main source of pension risk. It operates under trust deeds by which the corporate trustees are wholly owned subsidiaries of the Group. The trustee boards comprise seven directors selected by the Group and two directors nominated by members.

Risk appetite
Investment policy and related investment limits are agreed by the trustees with quantitative and qualitative input from the scheme actuaries and investment advisers. The trustees also consult with the Group to obtain its view on the appropriate level of risk within the pension funds. The Group independently monitors risk within its pension funds as part of the ICAAP including metrics focused on capital volatility incorporated in the overall risk appetite framework.

Risk mitigation
The trustee board is solely responsible for the investment of the scheme's assets which are held separately from the assets of the Group. The Group and the trustee board must agree on the investment principles and the funding plan. An Investment Review Committee is in place for the scheme, comprising Bank and trustee representatives, which has specific responsibility for scheme investment matters.

The schemes are invested in diversified portfolios of quoted and private equity, government and corporate fixed-interest and index-linked bonds, and other assets including property, derivatives and hedge funds.

Credit risk

Definition
Credit risk is the risk of financial loss due to the failure of a customer or counterparty to meet its obligation to settle outstanding amounts.

Sources of credit risk
The principal sources of credit risk for the Group are as follows:

Lending - the Group offers a number of lending products that involve an obligation to provide credit facilities to customers. To mitigate the risk of loss, security may be obtained in the form of physical collateral (such as commercial real estate assets and residential property) or financial collateral (such as cash and bonds). Exposures arising from leasing activities are also included.

Derivatives and securities financing - the Group enters into derivatives contracts and securities financing transactions. These result in counterparty credit risk, which is the risk of financial loss arising from the failure of a counterparty to meet obligations that vary in value by reference to a market rate or asset price. To mitigate the risk of loss, collateral and netting are used along with the additional legal rights provided under the terms of over-the-counter contracts.

Debt securities - the Group holds some debt securities for liquidity management purposes and is exposed to credit risk as a result.

Off-balance sheet products - the Group provides trade finance and guarantees for customers, as well as committed but undrawn lending facilities, and is exposed to credit risk as a result.

Other activities - the Group is exposed to settlement risk through its activities in foreign exchange, trade finance and payments.

Credit risk management function

Governance
As is standard practice in the industry, credit risk management activities are organised along two separate lines, wholesale and retail, reflecting the distinction between business types and consequent drivers of credit risk. Wholesale focuses on activities with institutional, corporate and SME customers. Retail covers personal customers, small businesses as well as personal lending activities in private banking. Nonetheless, many activities remain common to both business lines.

The activities of the Group's credit risk management function, which is led by the Chief Credit Officer, include:
- approving credit for customers;
- ensuring that credit risk is within the risk appetite set by the Board;
- managing concentration risk and credit risk control frameworks;
- developing and ensuring compliance with credit risk policies and mandatory procedures; and
- conducting assessments of provision adequacy.

24. Risk management - credit risk (continued)

Risk appetite
Risk appetite across all risk types is set by the Group's Board using specific quantitative targets under stress, including earnings volatility and capital adequacy. The credit risk frameworks take into account concentrations and sector/product limits at Bank-wide level and have been designed to reflect factors that influence the ability to meet those targets. Tools such as stress testing and economic capital are used to measure credit risk volatility and develop links between the credit risk appetite frameworks and risk appetite targets. The frameworks are supported by a suite of policies/mandatory procedures and transaction acceptance standards that set out the risk parameters within which businesses must operate.

Risk models
The Group uses the output of credit risk models in the credit approval process - as well as for ongoing credit risk assessment, monitoring and reporting - to inform credit risk appetite decisions. These models are divided into different categories:

Model	Calculation method	Wholesale	Retail
Probability of Default	Individual counterparty	Each customer is assigned a probability of default (PD) rating and corresponding grade. PD is calculated using a combination of quantitative inputs, such as recent financial performance, and qualitative inputs such as management performance and sector outlook.	Each customer account is scored and models are used to assign a PD rating. Inputs vary across portfolios and include both internal account and customer level data, as well as Application Score which includes data from the Irish Credit Bureau.
Loss Given Default	Individual counterparty	Loss given default (LGD) models estimate the amount that would not be recovered in the event of a customer default. When estimating LGD, the Group's models assess both borrower and facility characteristics, as well as any credit risk mitigants. The cost of collections and a time-discount factor for the delay in cash recovery are also incorporated.	
Exposure At Default	Individual counterparty	Exposure at default (EAD) models provide estimates of credit facility utilisation at the time of a customer default, recognising that customers may make further drawings on unused credit facilities prior to default or that exposures may increase due to market movements. Regulatory requirements stipulate that EAD must always be equal to, or higher, than current utilisation, though exposures can be reduced by a legally enforceable netting agreement.	
Economic Capital	Portfolio level	The credit economic capital model is a framework that allows for the calculation of portfolio credit loss distributions and associated metrics over a given risk horizon for a variety of business purposes. The model takes into account migration risk (the risk that credit assets will deteriorate in credit quality across multiple years), factor correlation (the assumption that groups of obligors share a common factor) and contagion risk (for example, the risk that the weakening of the sovereign's credit worthiness has a significant impact on the creditworthiness of a business operating in that country).	

Impact of credit model changes
The Group reviews and updates models on an ongoing basis in order to reflect the impact of more recent data, changes to products and portfolios, and new regulatory requirements.

Model changes affect year-on-year comparisons of risk measures in certain disclosures. Where meaningful, in commentary, differentiations are made between instances where movements in risk measures reflect the impact of model changes and those where such movements reflect changes in the size of underlying credit portfolios or their credit quality.

24. Risk management - credit risk (continued)

Risk models (continued)

The following table analyses the sensitivity of the Income Statement to key inputs to the credit risk models.

Metric	Sensitivity	2017 €m
Retail Probability of Default	1% movement in Good Book (across all segments)	17
Wholesale Probability of Default	1% movement in Good Book (across all segments)	14
Probability of Default - Combined	**1% movement in Good Book (across all segments)**	**31**
Wholesale Loss Given Default	1% movement in collective & latent LGD	2
Retail Loss Given Default	1% house price movement	13
Retail Loss Given Default	1% movement in cure rates	11
Retail Emergence Period(1)	1 month increase in Emergence Period	2
Wholesale Emergence Period(1)	1 month increase in Emergence Period	3
Emergence Period - Combined	**1 month increase in Emergence Period**	**5**

(1)The emergence period is the period between the occurrence of an impairment event and a loan being identified and reported as impaired.

Risk mitigation

Risk mitigation techniques are used in the management of credit portfolios across the Group, typically to mitigate credit concentrations in relation to an individual customer, a borrower group or a collection of related borrowers. Where possible, customer credit balances are netted against obligations. Mitigation tools applied can include: structuring a security interest in a physical or financial asset; use of credit derivatives, including credit default swaps, credit-linked debt instruments and securitisation structures; and use of guarantees and similar instruments (for example, credit insurance) from related and third parties. When seeking to mitigate risk, at a minimum the Group considers the following:

- the suitability of the proposed risk mitigation, particularly if restrictions apply;
- the means by which legal certainty is to be established, including required documentation, supportive legal opinions and the steps needed to establish legal rights;
- the acceptability of the methodologies to be used for initial and subsequent valuation of collateral, the frequency of valuations and the advance rates given;
- the actions which can be taken if the value of collateral or other mitigants is less than needed;
- the risk that the value of mitigants and counterparty credit quality may deteriorate simultaneously;
- the need to manage concentration risks arising from collateral types; and
- the need to ensure that any risk mitigation remains legally effective and enforceable.

For further information, refer to the sub-sections on wholesale credit risk mitigation and retail credit risk mitigation.

Counterparty credit risk

The Group mitigates counterparty credit risk arising from both derivatives transactions and repurchase agreements through the use of market standard documentation, enabling netting, and through collateralisation.

Amounts owed by the Group to a counterparty are netted against amounts the counterparty owes the Group, in accordance with relevant regulatory and internal policies. However, generally, this is only done if a netting agreement is in place. A legal opinion, to the effect that the agreement is enforceable in the relevant jurisdictions, is also required.

Collateral may consist of either cash or securities. Additional collateral may be called should the net value of the obligations to the Group rise or should the value of the collateral itself fall. The majority of agreements are subject to daily collateral calls with collateral valued using internal valuation methodologies.

The Group restricts counterparty credit exposures by setting limits that take into account the potential adverse movement of an exposure after adjusting for the impact of netting and collateral (where applicable).

24. Risk management - credit risk (continued)

Risk assessment and monitoring
Practices for credit stewardship - including credit assessment, approval and monitoring as well as the identification and management of problem debts - differ between the wholesale and retail portfolios. A key aspect of credit risk stewardship is ensuring that, when signs of impairment are identified, appropriate impairment provisions are recognised.

Impairment, provisioning and write-offs
In the overall assessment of credit risk, impairment, provisioning and write-offs are used as key indicators of credit quality.

Impairment
A financial asset is impaired if there is objective evidence that the amount, or timing, of future cash flows has been adversely affected. Days-past-due measures are typically used to identify evidence of impairment. In both wholesale and retail portfolios, a period of 90 days past due is used as an initial trigger. Other indicators of impairment include the borrower's financial condition; a forbearance event; a loan restructuring; the probability of bankruptcy; or evidence of diminished cash flows.

Provisioning
The amount of an impairment loss is measured as the difference between the asset carrying amount and the present value of the estimated future cash flows discounted at the financial asset's original effective interest rate. The current net realisable value of the collateral will be taken into account in determining the need for a provision. This includes cash flows from foreclosure (less costs of obtaining and selling the collateral), whether or not foreclosure is probable. Impairment provisions are not recognised where amounts due are expected to be settled in full on the realisation of collateral. The Group uses one of the following three methods to quantify the provision required: individual; collective; and latent, as set out below:

Provision method	**Customer type**	**Quantification method**	**Key factors considered**
Individual	Impaired, individually significant	Case-by-case assessment of future cash flows	• Customer and guarantor performance. • Value of collateral. • Future economic conditions based on factors available at the time.
Collective	Impaired but not individually significant, grouped into homogenous portfolios	Quantitative review of relevant portfolio	• Level of arrears. • Value of security. • Historical and projected cash recovery trends. • Current economic conditions. • Operational processes. • Latest cash collection profile.
Latent	Not impaired	PD% x LGD% x Drawn Balance x Emergence Period	• For wholesale and retail customers PD, LGD, Drawn balance and Emergence Period. • Portfolio-level emergence periods are based on products or businesses with similar homogenous characteristics. Emergence periods range from 120 to 365 days.

Write-offs
Impaired loans and receivables are written-off when there is no longer any realistic prospect of recovery of part, or the entire loan. For loans that are individually assessed for impairment, the timing of write-off is determined on a case-by-case basis. Such loans are reviewed regularly and write-offs may be prompted by bankruptcy, insolvency, forbearance and similar events.

Amounts recovered after a loan has been written-off are credited to the loan impairment charge for the period in which they are received.

Wholesale risk assessment
Before credit facilities are made available to customers, a credit assessment is undertaken with approval obtained through either auto-decisioning or by a manual sanctioning process, referred to as the Credit Authority Framework ("CAF"). This framework is applied across the Group for the setting, use and monitoring of the application of Credit Authorities.

24. Risk management – credit risk (continued)

Wholesale risk assessment (continued)
Credit authority is delegated relative to the individual's level of experience, knowledge and qualifications and must be supported by a clear business need. Only a small number of senior executives hold the highest authority provided under the CAF. Both business and credit approvers are accountable for the quality of each decision taken but the credit risk approver holds ultimate sanctioning authority. Credit approval levels are determined by considering the aggregate borrowing of the customer and their credit quality, for example, a larger facility from a weaker customer would require a more experienced sanctioner to approve the proposal.

Auto-decisioning is used for larger volume/lower value applications. The quality of the auto-decisions is kept under review to determine if adjustments need to be made to thresholds.

The Wholesale CAF is governed by policy and a related Mandatory Procedure. These detail:
- the rules of delegation of authority;
- specific types of sanctioning and the approval rules associated with them; and
- CAF monitoring requirements.

It is the Bank's policy that an oversight programme is in place, where a selection of each sanctioner's approvals are reviewed by their line manager to ensure that an excellent standard of consistent decision making exists. All authorities are also reviewed by the heads of the credit sanctioning teams on an annual basis to ensure that the authority has been appropriately used and examines whether the level should be reviewed, based on the individual performance for the following year.

When assessing credit risk the following must be considered at a minimum:
- the amount, terms, tenor, structure, conditions, purpose and appropriateness of all credit facilities;
- compliance with relevant credit policies, mandatory procedures and transaction acceptance standards;
- the customer's ability to meet obligations, based on an analysis of financial information;
- a review of payment and covenant compliance history;
- the customer's risk profile, including sector, sensitivity to economic and market developments and management capability;
- legal capacity of the customer to engage in the transaction;
- credit risk mitigation including requirements for valuation and revaluation. The customer's credit grade and the loss given default estimate for the facilities, including any expected changes;
- the requirement for the provision of financial information, covenants and/or monitoring formulae to monitor the customer's financial performance;
- refinancing risk - the risk of loss arising from the failure of a customer to settle an obligation on expiry of a facility through the drawdown of another credit facility provided by the Group or by another lender;
- consideration of other risks such as environmental, social and ethical, regulatory and reputational risks; and
- the portfolio impact of the transaction, including the impact on any credit risk concentration limits or agreed business risk appetite.

Where the customer is part of a group, the credit assessment considers aggregated credit risk limits for the customer group as well as the nature of the relationship with the broader group (e.g. parental support) and its impact on credit risk. Credit relationships are reviewed and credit grades (PD and LGD) re-approved annually.

The review process addresses borrower performance, including reconfirmation or adjustment of risk parameter estimates; the adequacy of security; compliance with terms and conditions; and refinancing risk.

Wholesale credit risk mitigation
The Group mitigates credit risk relating to wholesale customers through the use of netting, collateral and market standard documentation, depending on the nature of the counterparty and its assets. The most common types of mitigation are:
- *Commercial real estate*.
- *Other physical assets* - including stock, plant, equipment, machinery, vehicles, ships and aircraft. Such assets are suitable collateral only if the Group can identify, locate, and segregate them from other assets on which it does not have a claim. The Group values physical assets in a variety of ways, depending on the type of asset and may rely on balance sheet valuations in certain cases.
- *Receivables* - these are amounts owed to the Group's counterparties by their own customers. The Group values them after taking into account the quality of its counterparty's receivable management processes and excluding any that are past due.

24. Risk management – credit risk (continued)

Wholesale credit risk mitigation (continued)
All collateral is assessed case by case to ensure that it will retain its value independently of the provider. The Group monitors the value of the collateral and, if there is a shortfall, will seek additional collateral.

Commercial real estate valuations
The Group has a panel of chartered surveying firms that cover the spectrum of geography and property sectors in which the Group takes collateral. The Group has a programme that identifies suitable valuers for particular assets, all of whom must be Registered Valuers and Members or Fellows of the Institute of Chartered Surveyors (MRICS, FRICS) or Society of Chartered Surveyors Ireland (MSCSI, FSCSI). They are contracted through a single service agreement to ensure consistency of quality and advice. Valuations are commissioned when an asset is taken as security; a material increase in a facility is requested; or an event of default is anticipated or has occurred. Valuations are conducted in accordance with current regulatory requirements.

Problem debt management

Early problem identification
Each segment has defined early warning indicators (EWIs) to identify customers experiencing financial difficulty, and to increase monitoring if needed. EWIs may be internal, such as a customer's bank account activity, or external, such as a publicly-listed customer's share price. If EWIs show a customer is experiencing potential or actual difficulty, or if relationship managers or credit officers identify other signs of financial difficulty they may decide to classify the customer within the Risk of Credit Loss Framework.

Risk of Credit Loss framework
The framework focuses on wholesale customers whose credit profiles have deteriorated since origination. Expert judgement is applied by experienced credit risk officers to classify cases into categories that reflect progressively deteriorating credit risk to the bank. There are two classifications which apply to non-defaulted customers within the framework - Heightened Monitoring and Risk of Credit Loss. The framework also applies to those customers that have met the Group's default criteria.

Heightened Monitoring customers are performing customers who possess certain characteristics, which have led to material credit deterioration. Collectively, characteristics reflect circumstances that may affect the customer's ability to meet repayment obligations. Characteristics include trading issues, covenant breaches, material PD downgrades and past due facilities. Sector-specific characteristics also exist. Heightened Monitoring customers require pre-emptive actions (outside the customer's normal trading patterns) to return or maintain their facilities within the bank's current risk appetite prior to maturity.

Risk of Credit Loss customers are performing customers who have met the criteria for Heightened Monitoring and also pose a risk of credit loss to the bank in the next 12 months, should mitigating action not be taken or not be successful.

Concentration risk management
Four formal frameworks are used to manage wholesale credit concentration risk. These are Product/Asset class, Sector, Single Name and Country concentration risks. These risks and the limits set associated with them are assessed for appropriateness on a regular basis.

Product/asset class concentration framework - the Group manages certain lines of business where the nature of credit risk assumed could result in a concentration or a heightened risk in some other form. This will include specific credit risk types such as asset finance, settlement risk, sponsor owned corporates and products such as long-dated derivatives. Typically specific limits and thresholds are deployed to manage the credit risk inherent in these areas, which are subject to regular review.

Sector concentration - sector concentration risk arises from the potential for excessive exposure to exist to any one or combination of correlated industry sectors that could behave similarly under stressed conditions. Risk appetite and portfolio strategies are set at sector or sub-sector level in order to mitigate this potential risk where historic experience or trends in external factors or portfolio performance give cause for concern.

Single-name concentration
The single name concentration framework addresses the risk of outsized exposure to a borrower or borrower group. The framework includes elevated approval authority, additional reporting and monitoring and the requirement for plans to address excessive exposures.

24. Risk management – credit risk (continued)

Concentration risk management (continued)

Country concentration - is the risk of losses occurring as a result of either a country event or unfavourable country operating conditions. As country events may simultaneously affect all or many individual exposures to a country, country event risk is a concentration risk. It arises from possible economic or political events in each country to which the Group has exposure and from unfavourable conditions affecting daily operations in a country. Country risk exposure is predominantly in the Republic of Ireland and the UK, in line with its strategic focus on core customer markets and lack of international lending activity. The other material country risk exposure relates to liquid asset investments comprising high grade sovereign and supranational bonds (Germany, France and Netherlands).

The Bank actively manages its concentrations and aligns its appetite for future business to the scale of its activities. The single name concentration framework is regularly reviewed for appropriateness including:

- simplifying the framework to ensure it remains fit for purpose; and
- sizing limits appropriately for the Group's core customer base and future strategy.

Retail credit risk management

Retail credit risk management within the Group is conducted in line with the common policies, procedures, frameworks and models that apply across the RBS Group.

Risk appetite

The Group uses a credit risk appetite framework to control credit risk for its retail business. The framework sets limits that measure and control the quality of both existing and new business. The actual performance of each portfolio is tracked relative to these limits and action taken where necessary. These limits apply to a range of credit risk-related measures including expected loss of the portfolio, the expected loss in a given stress scenario, projected credit default rates and the LTV of retail mortgage portfolios.

Retail credit risk assessment

Retail lending entails making a large number of small-value loans. To ensure that these lending decisions are made consistently, the Group analyses credit information, including the historical debt servicing behaviour of customers with respect to both the Group and their other lenders. The Group then sets its lending rules accordingly, developing different rules for different products. The process is somewhat automated, with customers receiving a credit score that reflects a comparison of their credit profile with the rule set. For relatively high-value, complex personal loans, including all residential mortgage lending, specialist credit managers make the final lending decision, having considered the application in totality.

Retail risk mitigation

The Group takes collateral in the form of residential property to mitigate the credit risk arising from mortgages and home equity lending. The Group values residential property during the loan underwriting process by appraising properties individually. Collateral is valued based on management's expectation regarding ability to collect. The Group updates residential property values quarterly using the relevant residential property index, namely the Central Statistics Office residential property price index.

Retail problem debt management

The management of retail mortgage customers in financial difficulty has been developed considering both Code of Conduct on Mortgage Arrears ("CCMA") requirements and the steps outlined in the Mortgage Arrears Resolution Process ("MARP") ensuring that:

- Each customer's individual circumstances are taken account of while treating them in a consistent manner.
- The reason for non payment of arrears is established and a sustainable solution for the borrower is sought.

The extensive range of forbearance solutions made available to customers as part of Mortgage Arrears Resolution Strategies ("MARS") increases engagement options available to mortgage customers in financial difficulty with the twin aims of providing:

- Suitable customers with an appropriate vehicle to long term sustainability.
- Avenues for customers with unsustainable mortgages to exit their home in a way that minimises the impact to both the customer and the Bank.

Retail forbearance

Within the Bank forbearance generally occurs when the business grants a permanent or temporary concession to a customer. Forbearance is granted following an assessment of the customer's individual circumstances and ability to pay.

Where the customer met the loan terms prior to modification and there is a realistic expectation that the customer will adhere to forbearance terms, these loans may in certain restricted circumstances (including appropriate consideration of probation periods) be classified as performing loans.

24. Risk management – credit risk (continued)

Retail credit risk management (continued)

Forbearance (continued)

Identification of forbearance
Customers who contact the Bank directly because of financial difficulties, or who are already in payment arrears, may be granted forbearance. In the course of assisting customers, more than one forbearance treatment may be granted.

Forbearance options include, but are not limited to:

- **Payment concessions** - a temporary reduction in, or elimination of, the periodic (usually monthly) loan repayment is agreed with the customer. At the end of the concessionary period, forborne principal and accrued interest outstanding is scheduled for repayment over an agreed period. The Group also offers payment concessions in the form of discounted interest rates that involve the forgiveness of some interest.
- **Capitalisation of arrears** - the customer repays the arrears over the remaining term of the mortgage and returns to an up-to-date position.
- **Term extensions** - the maturity date of the loan is extended.
- **Interest only conversions** - the loan converts from principal and interest repayment to interest only repayment on a permanent or temporary basis.

For unsecured portfolios, payment plans can be arranged for customers in difficulty. Arrangements to facilitate the repayment of overdraft excesses or loan arrears are generally agreed dependent on affordability. Where repayment arrangements are not affordable, debt consolidation loans may be provided to customers.

The mortgage arrears information for retail accounts in forbearance and related provisions are shown in the table below:

	2017		2016	
Arrears status and provisions	**Balance €m**	**Provisions €m**	Balance €m	Provisions €m
No missed payments	**2,004**	**273**	2,723	339
1-3 months in arrears	**525**	**89**	638	90
>3 months in arrears	**1,857**	**530**	1,731	494
Total	**4,386**	**892**	5,092	923

The incidence of the main types of retail forbearance on the balance sheet as at 31 December 2017 is analysed below. Definitions are based on those used within the CBI forbearance guidelines.

	2017 €m	2016 €m
Interest only conversions - temporary and permanent	**238**	310
Term extensions – capital repayment & interest only	**361**	364
Payment concession/holidays	**2,779**	3,163
Capitalisation of arrears	**1,008**	1,255
Total	**4,386**	5,092

In the retail portfolio, loans are considered forborne until they meet the exit criteria set out by the European Banking Authority. These include being classified as performing for two years since the last forbearance event, making regular repayments and the debtor being less than 30 days past due.

Impairments for forbearance
The methodology used for provisioning and impairments for forborne loans will differ depending on whether the loans are performing or non-performing.

For the latent calculation, an extended emergence period is applied to account for the impact of forbearance within the portfolio. Additionally, for portfolios with material forbearance, forborne loans form a separate risk pool for calibration purposes.

For non-performing loans, forborne loans which result in an economic loss to the group form a separate risk pool where specific LGDs are allocated using observed performance of these loans.

24. Risk management - credit risk (continued)

Retail credit risk management (continued)

Recoveries

- Once a loan has been identified as impaired, it is managed by recoveries teams in the relevant businesses. The teams seek to minimise the Group's loss by maximising cash recovery while treating customers fairly.
- Where an acceptable repayment arrangement cannot be agreed with the customer litigation may be considered. Additionally, certain forbearance options are made available to customers managed by the recoveries function.

The following table shows the distribution of residential mortgages by loan-to-value (LTV) (indexed). LTV is based upon gross loan amounts and, whilst including defaulted loans, does not take account of provisions made.

	Group	
	2017	2016
Residential mortgages – distribution by average LTV [(1)]	**%**	%
<=50%	45.98	42.00
>50% and <=80%	32.47	29.20
>80% and <=100%	13.57	14.70
>100% and <=150%	7.77	13.70
>150%	0.21	0.40
Total portfolio average LTV at 31 December	54.17	58.98
Average LTV on new originations during the financial year	70.10	72.19

(1) The above table uses unweighted LTV averages calculated by transaction volume.

The tables below show period-end weighted LTVs for the Bank's residential mortgage portfolio:

2017 **LTV ratio value [(1)]**	**<=50%** **€m**	**50** **<=80%** **€m**	**80** **<=100%** **€m**	**100** **<=150%** **€m**	**>150%** **€m**	**Total** **€m**	**Weighted Average LTV** **%**
AQ1-AQ8	**3,956**	**5,630**	**2,354**	**987**	**17**	**12,944**	**63**
AQ9	**264**	**518**	**451**	**380**	**9**	**1,622**	**79**
Accruing past due/non-accrual	**375**	**692**	**655**	**966**	**44**	**2,732**	**87**
Total	**4,595**	**6,840**	**3,460**	**2,333**	**70**	**17,298**	**69**
2016							
AQ1-AQ8	3,322	4,834	2,559	2,074	16	12,805	70
AQ9	283	510	482	834	13	2,122	88
Accruing past due/non-accrual	330	635	578	1,301	106	2,950	95
Total	3,935	5,979	3,619	4,209	135	17,877	76

(1) LTV is calculated on a current exposure basis, gross of provisions.

The table below details residential mortgages three months or more in arrears (by volume):

	Group	
	2017	2016
Retail	**%**	%
Mortgages	**9.3**	8.7

Aside from the lending portfolios, the Group receives collateral and other credit enhancements on other financial assets on its balance sheet as detailed in the following table.

	2017	2016
	€m	€m
Derivative assets gross exposure	**341**	28

24. Risk management – credit risk (continued)

Asset quality (unaudited)

Internal reporting and oversight of risk assets is principally differentiated by credit grades. Customers are assigned credit grades based on various credit grading models that reflect the key drivers of default for each customer type. All credit grades across the Group map to both a Group level asset quality scale, used for external financial reporting, and a master grading scale for wholesale exposures, used for internal management reporting across portfolios. Accordingly, measures of risk exposure may be readily aggregated and reported at increasing levels of granularity depending on stakeholder or business need.

Performing loans are defined as AQ1-AQ9 (where the PD is less than 100%) and non performing loans as AQ10 (where the PD is 100%).The PD models used to assign a credit grade for the purposes of credit risk management assess the probability of a customer failing to honour its credit obligations over a one-year time period.

The table below shows the relationship between asset quality (AQ) band and PD.

AQ Band	Probability of default	Indicative S&P rating
AQ1	0% - 0.034%	AAA to AA
AQ2	0.034% - 0.048%	AA-
AQ3	0.048% - 0.095%	A+ to A-
AQ4	0.095% - 0.381%	BBB+ to BBB-
AQ5	0.381% - 1.076%	BB+ to BB
AQ6	1.076% - 2.153%	BB to B+
AQ7	2.153% - 6.089%	B+ to B
AQ8	6.089% - 17.222%	B- to CCC+
AQ9	17.222% - 100%	CCC to C
AQ10	100%	D

24. Risk management - credit risk (continued)

Asset quality (unaudited) (continued)

The following table provides, for wholesale and retail assets combined, a breakdown of the credit quality of third party financial assets by AQ band.

	Group					
2017	**Cash and balances at central banks €m**	**Loans and advances to banks €m**	**Loans and advances to customers €m**	**Derivatives €m**	**Commitments €m**	**Contingent liabilities €m**
AQ1	322	2,136	239	514	1	-
AQ2	-	-	-	-	-	-
AQ3	-	2,732	375	7	513	105
AQ4	-	24	3,807	23	1,073	88
AQ5	-	1	7,788	11	1,043	108
AQ6	-	-	3,453	27	554	61
AQ7	-	-	602	-	276	26
AQ8	-	-	430	-	27	5
AQ9	-	-	1,635	-	6	5
AQ10	-	-	-	-	23	19
Accruing past due	-	-	1,641	-	-	-
Non–accrual	-	-	3,244	-	-	-
Impairment provisions	-	-	(1,264)	-	-	-
Total	**322**	**4,893**	**21,950**	**582**	**3,516**	**417**

	Group					
2016	Cash and balances at central banks €m	Loans and advances to banks €m	Loans and advances to customers €m	Derivatives €m	Commitments €m	Contingent liabilities €m
AQ1	290	1,799	311	925	17	19
AQ2	-	-	-	-	79	-
AQ3	-	2,801	356	11	388	128
AQ4	-	21	3,431	42	1,082	100
AQ5	-	1	7,803	10	1,052	56
AQ6	-	-	3,453	37	551	43
AQ7	-	-	813	-	245	43
AQ8	-	-	450	-	37	4
AQ9	-	-	1,415	-	9	1
AQ10	-	-	-	-	50	23
Accruing past due	-	-	1,656	-	-	-
Non–accrual	-	-	3,718	-	-	-
Impairment provisions	-	-	(1,392)	-	-	-
Total	290	4,622	22,014	1,025	3,510	417

24. Risk management - credit risk (continued)

Asset quality (unaudited) (continued)

	Bank					
2017	**Cash and balances at central banks €m**	**Loans and advances to banks €m**	**Loans and advances to customers €m**	**Derivatives €m**	**Commitments €m**	**Contingent liabilities €m**
AQ1	322	2,136	653	486	1	-
AQ2	-	-	-	-	-	-
AQ3	-	2,732	375	7	513	105
AQ4	-	24	3,807	23	1,073	88
AQ5	-	1	7,788	11	1,043	108
AQ6	-	-	3,453	27	554	61
AQ7	-	-	602	-	276	26
AQ8	-	-	430	-	27	5
AQ9	-	-	1,635	-	6	5
AQ10	-	-	-	-	23	19
Accruing past due	-	-	1,641	-	-	-
Non–accrual	-	-	3,244	-	-	-
Impairment provisions	-	-	(1,264)	-	-	-
Total	**322**	**4,893**	**22,364**	**554**	**3,516**	**417**

	Bank					
2016	Cash and balances at central banks €m	Loans and advances to banks €m	Loans and advances to customers €m	Derivatives €m	Commitments €m	Contingent liabilities €m
AQ1	290	1,480	796	885	17	19
AQ2	-	-	-	-	79	-
AQ3	-	2,801	356	11	388	128
AQ4	-	21	3,431	42	1,082	100
AQ5	-	1	7,803	10	1,052	56
AQ6	-	-	3,453	37	551	43
AQ7	-	-	813	1	245	43
AQ8	-	-	450	-	37	4
AQ9	-	-	1,415	-	9	1
AQ10	-	-	-	-	50	23
Accruing past due	-	-	1,656	-	-	-
Non–accrual	-	-	3,718	-	-	-
Impairment provisions	-	-	(1,392)	-	-	-
Total	290	4,303	22,499	986	3,510	417

Loans and advances to customers, past due at balance sheet date but not considered impaired are shown in Note 10.

24. Risk management - credit risk (continued)

Credit risk concentrations

Credit risk assets by industry and geography
Industry analysis plays an important part in assessing the potential for concentration risk in the loan portfolio. Particular attention is given to industry sectors where the Group believes there is a high degree of risk or potential for volatility in the future.

The tables below analyse financial assets by geographical region (based on location of transaction office) and sector.

	Group				
	Gross loans and advances to banks and customers	**Debt securities and equity shares**	**Derivatives**	**Total**	**Netting and offset[1]**
2017	**€m**	**€m**	**€m**	**€m**	**€m**
Republic of Ireland					
Central and local government	28	1,170	-	1,198	-
Manufacturing	469	-	4	473	10
Construction	153	-	-	153	-
Finance	5,250	861	524	6,635	21
Service industries and business activities	2,492	-	53	2,545	49
Agriculture, forestry and fishing	553	-	-	553	7
Property	1,111	-	1	1,112	1
Individuals					
Home mortgages	17,317	-	-	17,317	-
Other	694	-	-	694	-
Interest accruals	14	12	-	26	-
Total Republic of Ireland	**28,081**	**2,043**	**582**	**30,706**	**88**
UK					
Service industries and business activities	20	-	-	20	-
Property	6	-	-	6	-
Total UK	**26**	**-**	**-**	**26**	**-**
Total					
Central and local government	28	1,170	-	1,198	-
Manufacturing	469	-	4	473	10
Construction	153	-	-	153	-
Finance	5,250	861	524	6,635	21
Service industries and business activities	2,512	-	53	2,565	49
Agriculture, forestry and fishing	553	-	-	553	7
Property	1,117	-	1	1,118	1
Individuals					
Home mortgages	17,317	-	-	17,317	-
Other	694	-	-	694	-
Interest accruals	14	12	-	26	-
	28,107	**2,043**	**582**	**30,732**	**88**

[1] For notes relating to this table refer to page 98.

24. Risk management - credit risk (continued)

Credit risk concentrations (continued)

Credit risk assets by industry and geography (continued)

	Group				
2016	Gross loans and advances to banks and customers €m	Debt securities and equity shares €m	Derivatives €m	Total €m	Netting and offset[(1)] €m
Republic of Ireland					
Central and local government	32	2,329	-	2,361	-
Manufacturing	470	-	6	476	3
Construction	211	-	-	211	6
Finance	4,952	-	949	5,901	28
Service industries and business activities	2,487	-	69	2,556	61
Agriculture, forestry and fishing	523	-	-	523	19
Property	925	-	1	926	2
Individuals					
Home mortgages	17,877	-	-	17,877	-
Other	474	-	-	474	-
Interest accruals	20	17	-	37	-
Total Republic of Ireland	27,971	2,346	1,025	31,342	119
UK					
Manufacturing	2	-	-	2	-
Service industries and business activities	47	-	-	47	-
Property	8	-	-	8	-
Total UK	57	-	-	57	-
Total					
Central and local government	32	2,329	-	2,361	-
Manufacturing	472	-	6	478	3
Construction	211	-	-	211	6
Finance	4,952	-	949	5,901	28
Service industries and business activities	2,534	-	69	2,603	61
Agriculture, forestry and fishing	523	-	-	523	19
Property	933	-	1	934	2
Individuals					
Home mortgages	17,877	-	-	17,877	-
Other	474	-	-	474	-
Interest accruals	20	17	-	37	-
	28,028	2,346	1,025	31,399	119

(1) This column shows the amount by which the Group's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Group a right to set-off the financial asset against a financial liability due to the same counterparty. Cash and securities are received as collateral in respect of derivative transactions.

24. Risk management - credit risk (continued)

Credit risk concentrations (continued)

Credit risk assets by industry and geography (continued)

	Bank				
2017	**Gross loans and advances to banks and customers** €m	**Debt securities and equity shares** €m	**Derivatives** €m	**Total** €m	**Netting and offset[1]** €m
Republic of Ireland					
Central and local government	28	1,170	-	1,198	-
Manufacturing	469	-	4	473	10
Construction	153	-	-	153	-
Finance	5,668	6,142	496	12,306	21
Service industries and business activities	2,488	-	53	2,541	49
Agriculture, forestry and fishing	553	-	-	553	7
Property	1,111	-	1	1,112	1
Individuals					
Home mortgages	17,317	-	-	17,317	-
Other	694	-	-	694	-
Interest accruals	14	12	-	26	-
Total Republic of Ireland	**28,495**	**7,324**	**554**	**36,373**	**88**
UK					
Service industries and business activities	20	-	-	20	-
Property	6	-	-	6	-
Total UK	**26**	**-**	**-**	**26**	**-**
Total					
Central and local government	28	1,170	-	1,198	-
Manufacturing	469	-	4	473	10
Construction	153	-	-	153	-
Finance	5,668	6,142	496	12,306	21
Service industries and business activities	2,508	-	53	2,561	49
Agriculture, forestry and fishing	553	-	-	553	7
Property	1,117	-	1	1,118	1
Individuals					
Home mortgages	17,317	-	-	17,317	-
Other	694	-	-	694	-
Interest accruals	14	12	-	26	-
	28,521	**7,324**	**554**	**36,399**	**88**

(1) For note relating to this table refer page 100.

24. Risk management - credit risk (continued)

Credit risk concentrations (continued)

Credit risk assets by industry and geography (continued)

	Bank				
	Gross loans and advances to banks and customers	Debt securities and equity shares	Derivatives	Total	Netting and offset[1]
2016	€m	€m	€m	€m	€m
Republic of Ireland					
Central and local government	32	2,329	-	2,361	-
Manufacturing	470	-	6	476	3
Construction	211	-	-	211	6
Finance	5,122	7,731	910	13,763	28
Service industries and business activities	2,483	-	69	2,552	61
Agriculture, forestry and fishing	523	-	-	523	19
Property	925	-	1	926	2
Individuals					
Home mortgages	17,877	-	-	17,877	-
Other	474	-	-	474	-
Interest accruals	20	17	-	37	-
Total Republic of Ireland	28,137	10,077	986	39,200	119
UK					
Manufacturing	2	-	-	2	-
Service industries and business activities	47	-	-	47	-
Property	8	-	-	8	-
Total UK	57	-	-	57	-
Total					
Central and local government	32	2,329	-	2,361	-
Manufacturing	472	-	6	478	3
Construction	211	-	-	211	6
Finance	5,122	7,731	910	13,763	28
Service industries and business activities	2,530	-	69	2,599	61
Agriculture, forestry and fishing	523	-	-	523	19
Property	933	-	1	934	2
Individuals					
Home mortgages	17,877	-	-	17,877	-
Other	474	-	-	474	-
Interest accruals	20	17	-	37	-
	28,194	10,077	986	39,257	119

(1)This column shows the amount by which the Bank's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Bank a right to set-off the financial asset against a financial liability due to the same counterparty. Cash and securities are received as collateral in respect of derivative transactions.

24. Risk management (continued)

Market risk

Definition
Market risk is the risk of losses arising from fluctuations in interest rates, credit spreads, foreign currency rates, equity prices, commodity prices and other factors, such as market-implied volatilities, that may lead to a reduction in earnings, economic value or both.

The principal market risks to which the Group is exposed to are non-trading interest rate and foreign exchange risks as a result of its retail and commercial banking activities. Traded market risk from customer derivative and foreign exchange activities is eliminated by entering into back-to-back positions with RBS plc.

The following disclosures in this section are audited:
- Traded market risk - Internal VaR.
- Non-traded market risk:
  - Interest rate VaR; and
  - Foreign exchange risk.

Sources of risk

Traded market risk
Traded market risk is limited to over-the-counter customer derivatives and foreign exchange transactions executed with the Markets business. Traded market risk is fully eliminated by a hedging programme executing back-to-back positions with RBS plc.

Non-traded market risk
The majority of non-traded market risk exposure arises from retail and commercial banking activities and from the High Quality Liquid Asset portfolio and investment of equity capital.

Non-traded market risk largely comprises interest rate risk and foreign exchange risk.

Interest rate risk
Non-traded interest rate risk ("NTIRR") arises from the provision to customers of a range of banking products that have differing interest rate characteristics and from non-interest bearing assets and liabilities on the balance sheet. When aggregated, these products form portfolios of assets and liabilities with varying degrees of sensitivity to changes in market interest rates. Mismatches in these characteristics can give rise to volatility in net interest income as interest rates vary.

NTIRR comprises three primary risk factors: gap risk, basis risk and option risk which are detailed further on page 103.

Credit spread risk
Credit spread risk arises from the potential adverse economic impact of a move in the spread between bond yields and swap rates, where the bond portfolios are accounted at fair value in the non-trading book.

Foreign exchange risk
Non-traded foreign exchange risk exposures arise from three main sources:
- **Structural foreign exchange risk** - arising from the capital deployed in branches and related currency funding where it differs from Euro.
- **Transactional foreign currency exposure** - arising from mismatches in the currency balance sheet.
- **Foreign currency profit streams and costs** - in respect of branches in the UK.

Equity risk
Non-traded equity risk is the potential variation in income and reserves arising from changes in the values of non-trading book equity positions. Equity exposures may arise through strategic acquisitions and certain restructuring arrangements.

Accounting volatility risk
Accounting volatility risk arises when a non-trading book exposure is accounted at amortised cost but economically hedged by a derivative that is accounted at fair value. Although this is not an economic risk, the difference in accounting between the exposure and the hedge creates volatility in the income statement.

Pension risk
Pension-related activities also give rise to market risk.

24. Risk management - market risk (continued)

Risk governance
Responsibility for identifying, measuring, monitoring and controlling the market risk arising from trading or non-trading activities lies with Markets and Treasury respectively, with independent oversight provided by the Market Risk function.

Market risk positions are reported monthly to ALCO and the Executive Risk Committee and quarterly to the Board Risk Committee. In addition, market risk maintains daily and monthly monitoring.

RBS Executive Risk Forum ("ERF") approves overall Group market risk limits. Market risk policy statements set out the governance and risk management framework through effective identification, measurement, reporting, mitigation, monitoring and control and are approved by ALCO.

The Group's policy is to manage risk exposures within an appetite that is set by the ERF and endorsed by ALCO. This appetite for UBIDAC is set and approved by the Board.

Risk appetite
The Group's qualitative market risk appetite is set out in policy statements.

Its quantitative market risk appetite is expressed in terms of limits for the non-trading activities that are consistent with business plans. De-minimis traded market risk limits are approved to cover any timing issues with booking the back-to-back hedging.

Market risk cascades the non-traded limits further down the organisation as required to Treasury desks. For each desk, a document known as a dealing authority compiles details of all applicable limits and trading restrictions.

The limit framework comprises VaR, stressed value-at-risk (SVaR) and sensitivity and stress limits.

The limits are reviewed to reflect changes in risk appetite, business plans, portfolio composition and the market and economic environments.

To ensure approved limits are not breached and that the Group remains within its risk appetite, triggers at the Group and lower levels have been set such that if exposures exceed a specified level, action plans are developed by the front office, Market Risk and Finance.

Risk identification and assessment
Identification and assessment of traded and non-traded market risk is achieved through gathering, analysing, monitoring and reporting market risk information by business line or at a consolidated level. Industry expertise, continued system developments and techniques such as stress testing are also used to enhance the effectiveness of the identification and assessment of all material market risks.

This is complemented by the New Product Risk Assessment process, which requires market risk teams to assess and quantify the market risk associated with all proposed new products.

Risk monitoring
Traded and non-traded Market Risk exposures are monitored against limits and analysed daily by market risk reporting and control functions and monthly in the case of structural interest rate risk.

The Market Risk function also prepares daily risk reports that detail exposures against a more granular set of limits and triggers. Limit reporting is supplemented with stress testing information as well as ad hoc reporting.

Risk measurement

The Group uses a comprehensive set of methodologies and techniques to measure traded and non-traded market risk.

The main risk measurement methods are VaR, SVaR, sensitivity and Earnings at Risk. Risks that are not adequately captured by VaR or SVaR are captured by the Risks not in VaR (RNIV) framework to ensure that the Group is adequately capitalised for market risk. In addition, stress testing is used to identify any vulnerabilities and potential losses in excess of VaR and SVaR.

The key inputs into these measurement methods are market data and risk factor sensitivities. Sensitivities refer to the changes in deal or portfolio value that result from small changes in market parameters that are subject to the market risk limit framework. Revaluation ladders are used in place of sensitivities to capture the impact on the income statement of large moves in risk factors or the joint impact of two risk factors.

24. Risk management – market risk (continued)

Risk measurement (continued)

These methods have been designed to capture correlation effects and allow the Group to form an aggregated view of its traded market risk across risk types, markets and business lines while also taking into account the characteristics of each risk type.

Risk assessment, monitoring and mitigation

Interest rate risk
Non-traded interest rate risk (NTIRR) factors are grouped into the following categories:

- Gap risk - which arises from the timing of rate changes in non-trading book instruments. The extent of gap risk depends on whether changes to the term structure of interest rates occur consistently across the yield curve (parallel risk) or differentially by period (non-parallel risk).
- Basis risk - which captures the impact of relative changes in interest rates for financial instruments that have similar tenors but are priced using different interest rate indices, or on the same interest rate indices but with different tenors.
- Option risk - which arises from option derivative positions or from optional elements embedded in assets, liabilities and/or off-balance sheet items, where the Group or its customer can alter the level and timing of their cash flows. Option risk can be further characterised into automatic option risk and behavioural option risk.

NTIRR can be measured from either an economic value-based or earnings-based perspective (or both). Value-based approaches measure the change in value of the balance sheet assets and liabilities over a longer timeframe, including all cash flows. Earnings-based approaches measure the potential short-term (generally one year) impact on the income statement of charges in interest rates.

The Group uses both approaches to quantify its interest rate risk: VaR as its value-based approach and sensitivity of net interest income (NII) as its earnings-based approach.

Calculation of regulatory capital
The Group capitalises non-traded market risk as part of the ICAAP. The approach combines both earnings based and economic value based methodologies, in accordance with regulatory guidelines. The calculation captures the principal sources of non-traded market risk – interest rate risk, credit spread risk, structural foreign exchange risk and accounting volatility risk.

Pillar 1 capital must be held for non-trading book foreign exchange exposures, as outlined under CRR Articles 455 and 92(3)c. Structural foreign exchange exposures are excluded from the calculations as outlined under CRR Article 352(2); such exposures are considered under Pillar 2A.

Total VaR

The total VaR for the Group's dealing is presented in the table below:

	31 December 2017 **€m**	**Maximum** **€m**	**Minimum** **€m**	**Average** **€m**
Value-at-Risk	**0.9**	**1.3**	**0.6**	**0.9**

	31 December 2016 €m	Maximum €m	Minimum €m	Average €m
Value-at-Risk	1.1	2.0	0.5	1.0

Interest Rate VaR
The Interest Rate VaR limit is a sub limit of the Total VaR limit and is monitored daily.

Interest Rate VaR is presented in the table below:

	31 December 2017 **€m**	**Maximum** **€m**	**Minimum** **€m**	**Average** **€m**
Value-at-Risk	**0.7**	**0.9**	**0.6**	**0.7**

	31 December 2016 €m	Maximum €m	Minimum €m	Average €m
Value-at-Risk	1.0	1.6	0.5	0.9

25. Memorandum items

Contingent liabilities and commitments

The amounts shown in the table below are intended only to provide an indication of the volume of business outstanding at 31 December 2017. Although the Group is exposed to credit risk in the event of non-performance of the obligations undertaken by customers, the amounts shown do not, and are not intended to, provide any indication of the Group's expectation of future losses.

	Group and Bank	
	2017	2016
	€m	€m
Contingent liabilities:		
Guarantees and assets pledged as collateral security [(1)]	**154**	179
Other contingent liabilities	**263**	238
	417	417
Commitments:		
Documentary credits and other short-term trade related transactions	**2**	2
Commitments to lend	**3,494**	3,484
Other commitments	**20**	24
	3,516	3,510

(1) The amount of guarantees and assets pledged as collateral security includes €nil in 2017 (2016: €31m) incurred on behalf of or for the benefit of fellow subsidiary undertakings

Banking commitments and contingent obligations, which have been entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities. The Group's maximum exposure to credit loss, in the event of non-performance by the other party and where all counterclaims, collateral or security proves valueless, is represented by the contractual nominal amount of these instruments included in the table. These commitments and contingent obligations are subject to the Group's normal credit approval processes.

Contingent liabilities

Guarantees - the Group gives guarantees on behalf of customers. A financial guarantee represents an irrevocable undertaking that the Group will meet a customer's obligations to third parties if the customer fails to do so. The maximum amount that the Group could be required to pay under a guarantee is its principal amount as disclosed in the table above. The Group expects most guarantees it provides to expire unused.

Regulatory enquiries and investigations - in the normal course of business the Bank and its subsidiaries co-operate with regulatory authorities in their enquiries or investigations into alleged or possible breaches of regulations.

Other contingent liabilities - these include standby letters of credit, supporting customer debt issues and contingent liabilities relating to customer trading activities such as those arising from performance and customs bonds, warranties and indemnities.

Additional contingent liabilities arise in the normal course of the Group's business. It is not anticipated that any material losses will arise from these transactions.

Commitments

Commitments to lend - under a loan commitment the Bank agrees to make funds available to a customer in the future. Loan commitments, which are usually for a specified term may be unconditionally cancellable or may persist, provided all conditions in the loan facility are satisfied or waived. Commitments to lend include commercial standby facilities and credit lines, liquidity facilities to commercial paper conduits and unutilised overdraft facilities.

Other commitments - these include documentary credits, which are commercial letters of credit providing for payment by the Group to a named beneficiary against presentation of specified documents, forward asset purchases, forward deposits placed and undrawn note issuance and revolving underwriting facilities, documentary credits and other short-term trade related transactions.

25. Memorandum items (continued)

Commitments (continued)
The Bank has given guarantees on the liabilities of the following subsidiary undertakings in accordance with the provision of Section 357 of the Companies Act 2014 and these entities will avail of the exemptions under Section 357 regarding the provisions of Sections 347 and 348.

Easycash (Ireland) Limited
First Active Insurances Services Limited
First Active Investments No.4 Limited
Hume Street Nominees Limited
Norgay Property Limited
The RBS Group Ireland Retirement Savings Trustee Limited
Walter Property Limited

Contractual obligations for future expenditure not provided in the financial statements

The following table shows contractual obligations for future expenditure not provided for in the financial statements at the financial year end:

	Group and Bank	
	2017	2016
	€m	€m
Contracts to purchase goods or services	**4**	5

Litigation and investigations

The Group is involved in litigation, investigations and reviews in the United Kingdom and the Republic of Ireland. Other than as set out below, the litigation involves claims by and against Group companies which arise in the ordinary course of business. No material adverse effect on the net assets of the Group is expected to arise from the ultimate resolution of these claims. The material litigation, investigations and reviews involving the Group are described below. These matters could, individually or in the aggregate, have a material adverse effect on the Group's consolidated net assets, operating results or cash flows in any particular period.

FCA review of RBS's treatment of SMEs
The Skilled Person delivered its final report to the FCA during September 2016. In November 2016, the FCA published an update on its review. In response, RBS announced steps that will impact SME customers in the UK and the Republic of Ireland that were in GRG between 2008 and 2013. These steps were (i) an automatic refund of certain complex fees; and (ii) a new complaints process, overseen by an Independent Third Party. These steps have been developed with the involvement of the FCA which agreed that they were appropriate for RBS to take. UBIDAC estimates the costs associated with the new complaints review process and the automatic refund of complex fees to be approximately €11m, which was recognised as a provision in 2016. This includes operational costs together with the cost of refunded complex fees and the additional estimated redress costs arising from the complaints process.

On 23 October 2017, the FCA published an interim account incorporating a summary of the Skilled Person's report which stated that, further to the general investigation announced in November 2016, the FCA had decided to carry out a more focused investigation. The FCA published its final summary of the Skilled Person's report on 28 November 2017.

Review and investigation of treatment of tracker mortgage customers
In December 2015, the CBI announced that it had written to a number of lenders requiring them to put in place a robust plan and framework to review the treatment of customers who have been sold mortgages with a tracker interest rate or with a tracker interest rate entitlement. The CBI stated that the intended purpose of the review was to identify any cases where customers' contractual rights under the terms of their mortgage agreements were not fully honoured, or where lenders did not fully comply with various regulatory requirements and standards regarding disclosure and transparency for customers. The CBI has required the Group to participate in this review and the Group is co-operating with the CBI in this regard. The Group submitted its phase 2 report to the CBI on 31 March 2017, identifying impacted customers. The redress and compensation phase (phase 3) commenced in Q4 2017.

The Group has provisions totalling €223 million for this matter, including an additional provision of €87 million in 2017. Of the €298 million cumulative provision, €75 million had been utilised by 31 December 2017.

Separately, on 15 April 2016, the CBI notified UBIDAC that it was also commencing an investigation under its Administrative Sanctions Procedure into suspected breaches of the Consumer Protection Code 2006 during the period 4 August 2006 to 30 June 2008 in relation to certain customers who switched from tracker mortgages to fixed rate mortgages. This investigation is ongoing and the Group continues to co-operate with the CBI.

26. Net cash flow from operating activities

	Group		Bank	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
Net cash flow from trading activities	**(104)**	(2,774)	**(122)**	(2,430)
Decrease in loans and advances to banks and customers	**179**	3,677	**249**	3,571
Decrease in debt securities	**118**	2	**2,568**	1,580
(Increase)/decrease in other assets	**(9)**	68	**1**	68
Decrease/(increase) in derivative assets	**443**	(130)	**432**	(167)
Changes in operating assets	**731**	3,617	**3,250**	5,052
Increase/(decrease) in deposits by banks and customers	**1,683**	1,445	**(2,207)**	(560)
(Decrease)/increase in other liabilities	**(85)**	116	**(87)**	117
(Decrease)/increase in derivative liabilities	**(447)**	239	**(147)**	(13)
Changes in operating liabilities	**1,151**	1,800	**(2,441)**	(456)
Total taxes paid	**(3)**	(3)	**(2)**	(2)
Net cash inflow from operating activities	**1,775**	2,640	**685**	2,164

27. Interest received and paid

	Group		Bank	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
Interest received	**556**	590	**573**	632
Interest paid	**(107)**	(116)	**(253)**	(302)
	449	474	**320**	330

28. Analysis of changes in financing during the financial year

	Group					
	Share capital and share premium		Subordinated liabilities		Debt securities in issue	
	2017	2016	**2017**	2016	**2017**	2016
	€m	€m	**€m**	€m	**€m**	€m
At 1 January	**4,734**	4,734	**719**	725	**1,377**	2,005
Net cash flows from financing	**-**	-	**(100)**	-	**(1,377)**	(628)
Currency translation and other adjustments	**-**	-	**(3)**	(6)	**-**	-
At 31 December	**4,734**	4,734	**616**	719	**-**	1,377

	Bank			
	Share capital and share premium		Subordinated liabilities	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
At 1 January	**4,734**	4,734	**719**	725
Net cash flows from financing	**-**	-	**(100)**	-
Currency translation and other adjustments	**-**	-	**(3)**	(6)
At 31 December	**4,734**	4,734	**616**	719

29. Analysis of cash and cash equivalents

	Group		Bank	
	2017	2016	**2017**	2016
	€m	€m	**€m**	€m
At 1 January				
Cash	**814**	805	**497**	347
Cash equivalents	**4,152**	3,458	**4,151**	3,457
	4,966	4,263	**4,648**	3,804
Net cash inflow	**514**	707	**832**	848
Effect of exchange rate changes on cash and cash equivalents	**(9)**	(4)	**(9)**	(4)
At 31 December	**5,471**	4,966	**5,471**	4,648
Comprising:				
Cash and balances at central banks	**322**	290	**322**	290
Debt securities	**295**	177	**295**	177
Loans and advances to banks	**4,854**	4,499	**4,854**	4,181

30. Segmental analysis

The Group operates in the financial services industry in the Republic of Ireland and the United Kingdom and provides an integrated service to its customers. The directors manage the Group primarily by class of business and present the segmental analysis on that basis. Divisions charge market prices for services rendered to other parts of the Group; funding charges between divisions are determined by Group Treasury, having regard to commercial demands.

The Group reports on a segmental basis as follows:

Retail Banking, including Business Direct customers, provides loan and deposit products through a network of branches and direct channels.

Commercial Banking provides services to business and corporate customers.

Other represents central functions comprising Group and corporate functions such as Treasury, Finance, Risk, Legal, Customer Debt Solutions, Communications and Human Resources which support the Retail Banking and Commercial Banking divisions.

Class of Business — **Group**

	Total income						
	Net interest income	**Non-interest income**	**Total**	**Operating expenses before depreciation**	**Depreciation and amortisation**	**Impairment (loss)/gain**	**Operating loss before tax**
2017	**€m**	**€m**	**€m**	**€m**	**€m**	**€m**	**€m**
Retail Banking	350	123	473	(144)	-	(84)	245
Commercial Banking	128	75	203	(40)	-	16	179
Other	(7)	(60)	(67)	(513)	(12)	-	(592)
Total	**471**	**138**	**609**	**(697)**	**(12)**	**(68)**	**(168)**

Class of Business — **Group**

	Total income						
	Net interest income	Non-interest income	Total	Operating expenses before depreciation	Depreciation and amortisation	Impairment gain	Operating profit before tax
2016	€m	€m	€m	€m	€m	€m	€m
Retail Banking	376	103	479	(296)	-	19	202
Commercial Banking	123	79	202	(55)	-	119	266
Other	(10)	(5)	(15)	(411)	(10)	-	(436)
Total	489	177	666	(762)	(10)	138	32

30. Segmental analysis (continued)

	Group			
Class of Business	**2017**		2016	
	Assets	**Liabilities**	Assets	Liabilities
	€m	**€m**	€m	€m
Retail Banking	**17,450**	**10,701**	17,759	10,127
Commercial Banking	**4,999**	**9,511**	4,737	9,306
Other	**7,799**	**3,633**	8,198	4,773
Total	**30,248**	**23,845**	30,694	24,206

	Group					
Geographical analysis	**2017**			2016		
	Republic of Ireland	**United Kingdom**	**Total**	Republic of Ireland	United Kingdom	Total
	€m	**€m**	**€m**	€m	€m	€m
Total Income	**606**	**3**	**609**	656	10	666
Operating (loss)/profit before tax	**(170)**	**2**	**(168)**	22	10	32
Net assets/(liabilities)	**6,692**	**(289)**	**6,403**	6,665	(177)	6,488
Total assets	**30,221**	**27**	**30,248**	30,638	56	30,694

31. Transactions with directors

Transactions, agreements entered into by authorised institutions in respect of loans to persons who were directors of the Bank (or persons connected with them) at any time during the financial period were as follows:

Directors

	Principal and interest				
Name of director	As at 1 January (or date of appointment if later) €	As at 31 December €	Maximum outstanding amount during the financial year €	Interest due but not yet paid €	Provision €
2017					
D O'Shea [(1)]	485,991	446,372	486,114	-	-
2016					
D O'Shea [(1)]	525,283	485,991	525,283	-	-

(1) Mortgage loans held at commercial interest rates. During the period €39,619 (2016: €39,291) was repaid.

Connected parties

Pursuant to the provisions of the Companies Act 2014 the amounts required to be disclosed are as follows:
- the aggregate amounts outstanding as at 31 December 2017 were €1,753,017 (2016: €127,671),
- the aggregate maximum amounts outstanding during the period were €1,920,711 (2016: €169,475),
- the number of relevant persons for or with whom relevant transactions as at 31 December 2017 were made by the institution was 4 (2016: 3), and
- the maximum number of relevant persons for or with whom relevant transactions, arrangements and agreements that subsisted at any time during the period were made by the institution was 4 (2016: 3).

There were no guarantees, security or arrangements involving a guarantee or security entered into by authorised institutions in the Group in respect of guarantees to persons who were directors of the Bank (or persons connected with them) at any time during the financial period (2016: €nil).

At 31 December 2017, the total amount outstanding under any arrangement by the Bank with any director or person connected to a director was less than 10% of the Bank's total assets.

There were no amounts outstanding at 31 December 2017 (2016: €nil) in respect of loans made to directors by subsidiary undertakings which were not authorised institutions.

32. Directors' and secretary's interest in shares

At 31 December 2017, the directors and secretary did not have any interest in the shares or debentures of the ultimate holding company representing more than 1% of the nominal value of its issued share capital.

33. Related parties

The Bank's immediate parent company is Ulster Bank Holdings (ROI) Limited.

The Bank's ultimate holding company, and the parent of the largest group into which the Bank is consolidated, is RBS Group which is incorporated in Great Britain and registered in Scotland. Copies of the consolidated financial statements for RBS Group can be obtained from The Secretary, The Royal Bank of Scotland Group plc, Gogarburn, Edinburgh, EH12 1HQ, or at www.rbs.com.

For the financial year ended 31 December 2017 the smallest subgroup into which the Bank is consolidated is The Royal Bank of Scotland plc, a company incorporated in Great Britain and registered in Scotland. Copies of the consolidated financial statements for RBS Group can be obtained from The Secretary, The Royal Bank of Scotland plc, Gogarburn, Edinburgh, EH12 1HQ, or at www.rbs.com.

UK Government

The UK Government through HM Treasury is the ultimate controlling party of The Royal Bank of Scotland Group plc. Its shareholding is managed by UK Financial Investments Limited, a company it wholly owns and as a result, the UK Government and UK Government controlled bodies are related parties of the Group.

The following table details active related undertakings incorporated in the Republic of Ireland which are 100% owned by the Bank and fully consolidated for accounting purposes.

Entity name	Activity[1]
Easycash (Ireland) Limited	SC
First Active Insurances Services Limited	BF
First Active Investments No. 4 Limited	INV
First Active Limited	BF
Hume Street Nominees Limited	OTH
Norgay Property Limited	INV
The RBS Group Ireland Retirement Savings Trustee Limited	TR
Walter Property Limited	INV
Ulster Bank Pension Trustees (RI) Limited	OTH

The following table details related undertakings incorporated in the Republic of Ireland that are not active but fully consolidated includes entities where Bank ownership was less than 100%.

Entity name	Activity [1]	Accounting treatment [2]	Group Interest %
Ulster Bank Group Treasury Limited	INV	FC	100
UB SIG (ROI) Limited	INV	FC	100
Ulster Bank Wealth Unlimited Company	BF	FC	100
Qulpic Limited	INV	FC	67
West Register (Republic of Ireland) Property Limited	INV	FC	100
Zrko Limited	INV	FC	67

33. Related parties (continued)

The following table details related undertakings incorporated in the Republic of Ireland that are active. The Bank does not own any shares in the companies but their activities are conducted on behalf of the Bank and it retains the majority of the residual risks and benefits related to their activities. The results of the companies are therefore fully consolidated in the Group financial statements.

Entity name	Activity (1)	Accounting treatment (2)	Group Interest %
Celtic Residential Irish Mortgage Securitisation No. 14 Designated Activity Company	BF	FC	0
Celtic Residential Irish Mortgage Securitisation No. 15 Designated Activity Company	BF	FC	0

Notes:

(1) Activity - Banking and Financial institution (BF), Other/non-financial (OTH), Service Company (SC), Investment (shares or property) holding company (INV), Trustee (TR)

(2) Accounting treatment - Fully consolidated (FC), Investment Accounting (IA)

There are securitisation companies in which the Bank does not hold any of the voting rights but the activities of those companies are conducted on behalf of the Bank and it retains the majority of the residual ownership risks and benefits related to their activities. Therefore in accordance with the requirements of IFRS 10 the results of these securitisation companies are included in the Group's consolidated financial statements.

During the financial year the Group had the following transactions with related parties:

(a) Directors and key management

At 31 December 2017, amounts advanced by the Bank were €453,029 in respect of loans to 2 persons who served as directors during the financial period.

The aggregate transactions between the Bank and its directors, key management, their close families and companies which they control were:

	Number of directors	Number of key management	Connected parties	Transaction €
Transactions during the financial year				
Loans made during the financial year:				
- at a commercial rate	-	-	1	1,528,351
Balances outstanding at the end of the financial year				
Loans:				
- at a commercial rate	2	4	7	3,234,245
- at a preferential rate	-	1	-	626
Customer accounts:				
- Savings	4	8	22	2,239,188

33. Related parties (continued)

(b) Related party transactions

Included in the Group and Bank's balance sheet are the following balances with related parties at the financial year end:

	Group		Bank	
	2017	2016	**2017**	2016
Assets	**€m**	€m	**€m**	€m
Loans and advances:				
Parent companies	**2,136**	1,799	**2,135**	1,480
Key management	**1**	2	**1**	2
Other related parties, including fellow subsidiaries	**240**	160	**6,137**	8,772
	2,377	1,961	**8,273**	10,254
Equity shares:				
Other	**5**	6	**5**	6
Derivatives:				
Parent companies	**514**	916	**486**	877
Total assets	**2,896**	2,883	**8,764**	11,137
Liabilities				
Deposits:				
Parent companies	**488**	147	**486**	146
Key management	**2**	3	**2**	3
Other related parties, including fellow subsidiaries	**50**	142	**5,755**	9,737
	540	292	**6,243**	9,886
Subordinated loans:				
Parent companies	**530**	614	**530**	614
Other related parties, including fellow subsidiaries	**-**	16	**-**	16
	530	630	**530**	630
Derivatives:				
Parent companies	**394**	740	**159**	204
Total liabilities	**1,464**	1,662	**6,932**	10,720

(c) Compensation of key management

The aggregate remuneration of directors and other members of key management during the financial year was as follows:

	Group	
	2017	2016
	€	€
Short term benefits	**3,861,418**	4,048,276
Termination benefit	**-**	289,484
Long term benefits	**300,129**	509,322
Share-based benefits	**283,435**	157,843
Post-employment benefits	**141,688**	164,773
	4,586,670	5,169,698

34. Post balance sheet events

In January 2018 the directors declared and paid an interim dividend of €1,500 million.

35. Date of approval

The financial statements were approved by the Board of Directors on 16 February 2018.

36. Capital resources - unaudited

Capital regulation

The EU adopted legislative package, known as CRD IV consists of the Capital Requirements Regulation ("CRR") which is directly applicable across firms in the EU, and the new Capital Requirements Directive ("CRD"), which has been implemented by member states of the European Economic Area through national law. CRD IV is designed to strengthen the regulation of the banking sector and to implement the Basel III agreement in the EU legal framework.

The Bank Recovery and Resolution Directive ("BRRD") marks another step by European authorities in improving the stability of the financial system. The new framework is intended to enable resolution authorities to resolve failing banks with a lower risk of triggering contagion to the broader financial system, while sharing the costs of resolution with bank shareholders and creditors. To achieve this objective, the BRRD includes explicit provisions for the 'bail-in' of senior creditors where necessary.

Capital management

The objectives of the Bank's capital management and risk appetite framework are to at all times comply with the regulatory and internal capital requirements and to ensure that the Bank has sufficient capital to cover the current and future risks inherent in its business and to support its future development.

The Bank achieves this through the ICAAP process. The ICAAP is an internal assessment of capital that the Bank undertakes to ensure it is appropriately capitalised for its risk profile. The purpose of the ICAAP is to formalise the Bank's approach to understanding its risk profile and the processes and systems it needs to have in place to assess, quantify and monitor these risks.

The primary objective of the ICAAP is to ensure the Bank has adequate and appropriate capital to cover all material risks to which it is or may be exposed, at present or in the future. The Bank has in place a risk management framework to ensure that the identification and evaluation of those risks is comprehensive.

In support of the ICAAP, the Bank embeds risk management processes (Material Risk Assessment, Risk Appetite, Stress Testing and Capital Planning), which are integrated into the wider risk management processes in the Bank including ILAAP, liquidity planning and recovery planning, ensuring effective management of the risk profile of the Bank.

36. Capital resources - unaudited (continued)

The Capital Requirements Regulation (CRR) and Capital Requirements Directive (CRD IV - which was enacted in Irish law by S.I. No. 158 of 2014 and S.I. No. 159 of 2014) requirements are being implemented on a phased basis from 1 January 2014, with full implementation from 1 January 2019. The capital resources disclosures for 2017 below reflect the transition arrangements of the legislation together with the CBI guidance (Implementation of Competent Authority Discretions and Options in CRD IV and CRR) on the application of transitional rules in Ireland.

	Unaudited[(1)] 2017 €m	Unaudited[(1)] 2016 €m
Shareholders' equity (excluding non-controlling interests)	**6,403**	6,487
Non-controlling interests		
Non-controlling interests per balance sheet	**-**	1
Other adjustments to non-controlling interests for regulatory purposes	**-**	(1)
	-	-
Regulatory adjustments and deductions		
Own Credit	**(1)**	(3)
Defined benefit pension fund adjustment	**(44)**	71
Deferred tax assets	**(88)**	(59)
Excess of expected losses over impairment provisions	**(120)**	(116)
Goodwill and other intangible assets	**(1)**	-
Qualifying deductions exceeding AT1 capital	**(15)**	(39)
Other regulatory adjustments	**41**	(79)
	(228)	(225)
Core tier 1 capital	**6,175**	6,262
Deductions		
Excess of expected losses over impairment provisions	**(15)**	(39)
Qualifying deductions exceeding AT1 capital	**15**	39
Total tier 1 capital	**6,175**	6,262
Qualifying tier 2 capital		
Paid up capital instruments and subordinated loans	**534**	649
Tier 2 deductions		
Residual amount for shortfall of provisions to expected loss	**(15)**	(39)
	(15)	(39)
Total tier 2 capital	**519**	610
Total regulatory capital	**6,694**	6,872
Key capital ratios	**%**	%
Tier 1	**31.2**	29.8
Total capital	**33.8**	32.7
Risk weighted assets by risk		
Credit risk	**18,116**	18,987
Counterparty risk	**362**	589
Market risk	**76**	14
Operational risk	**1,240**	1,419
Total risk weighted assets	**19,794**	21,009

(1) The capital metrics included in the above table have not been audited for the financial years ended 31 December 2017 and 31 December 2016.

36. Capital resources - unaudited (continued)

In the management of capital resources, the Bank is governed by the UBIDAC and RBS policies which are to maintain a strong capital base, to expand it as appropriate and to utilise it efficiently throughout its activities to optimise the return to shareholders while maintaining a prudent relationship between the capital base and the underlying risks of the business.

In carrying out these policies the Bank has regard to and has complied with the capital supervisory requirements of the ECB and CBI throughout the financial year.

37. Non-performing exposures - unaudited

A non-performing exposure (NPE), as defined by the European Banking Authority ("EBA"), is a credit exposure:

- that is considered to be impaired; or
- that is in default; or
- that is a material exposure that is more than 90 days past-due; or
- where the debtor is assessed as unlikely to fulfil the credit obligations in full without realisation of collateral regardless of the existence of any past-due amount or number of days past-due; or
- that is an exposure to a debtor where more than 20% of the on-balance sheet exposures to that debtor are more than 90 days past due (the pulling effect); or
- that is a performing forborne contract under probation that is extended additional forbearance measures or becomes more than 30 days past-due (there is a 2 year probation period from the date that a forborne exposure is classified as performing before classification as forborne can be discontinued).

NPEs include financial instruments at amortised cost, financial instruments at fair value other than held-for-trading and off balance sheet exposures.

An exposure is no longer considered to be non-performing when it is not impaired, not in default and has no amount past due by more than 90 days; however a non-performing exposure that has been extended forbearance must be classified as non-performing for a minimum of 12 months with consideration taken of the financial situation of the debtor before classification as performing. Following the forbearance measures, there is not any past-due amount regarding the full repayment of the exposure according to the post forbearance conditions.

The additional criteria that distinguish NPEs from impaired loans mean that the Group's NPEs must by definition be greater than the impaired loans. These include the mandatory 12 month classification of forborne balances as non-performing, the 20% pulling effect, that consideration is not given to collateral in the determination of non-performing exposures, the 90 days past-due automatic threshold for designation as non-performing for non-forborne balances and the 30 days past-due threshold for performing forborne balances under probation. Under IAS 39 the past-due more than 90 days exposures would all be assessed for impairment.

The table below shows the Group's NPEs at the balance sheet date.

	Group	
	2017	2016
	€m	€m
Non-performing exposures	**4,330**	4,754
- of which are impaired	***3,244***	*3,718*