Bank of Ireland (UK) plc Annual Report

For the year ended
31 December 2013

For small steps, for big steps, for life

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UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:31 Page 1

Bank of Ireland (UK) plc
Annual Report

For the year ended 31 December 2013

Company Number: 07022885

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:31 Page 2

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UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:31 Page 1

Contents

Business Review

Chairman's Statement 2
Strategic Report 3

Risk Management

Risk Management Framework 24
Credit Risk 29
Financial Risk 49

Governance

Directors and Other Information 57
Report of the Directors 60

Financial Statements

Statement of Directors' Responsibilities 62
Independent Auditors' Report 63
Consolidated Financial Statements and Notes 64
Bank Financial Statements and Notes 133

Other Information

Principal Business Units and Addresses 162
Abbreviations 163

Chairman's Statement

Bank of Ireland (UK) plc "the Bank" is the principal operating subsidiary of the Bank of Ireland Group in the UK. It was formed at the end of 2010 as a Bank operating within the Bank of Ireland Group but separately capitalised, with its own governance and independently regulated by the Prudential Regulation Authority and Financial Conduct Authority in the UK.

In its first two years, during difficult economic and market conditions, the Bank concentrated on building its own capabilities, on renewing and extending its core financial services partnership with the Post Office and on positioning its business towards a viable and sustainable future.

I am pleased to be able to report that 2013 has been a year of positive transition for the Bank. Our profits have shown a significant recovery, though our return on capital at 2.8% is not yet sufficient. We have had to make difficult pricing decisions affecting both our lending and deposit customers which have resulted in an improvement in net interest margin. The burden of impairment charges, particularly relating to historic property related lending, has also eased appreciably.

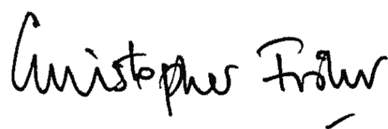
The relationship with our core partner, the Post Office, continues to develop and deepen. We have shared ambitions to build a successful and broadly-based financial services offering for Post Office customers. We already have some 2.7 million such customers, and well established existing deposit taking, foreign exchange and ATM services. We have positioned ourselves to make significant progress in the period ahead in relation to mortgages, credit and travel cards and insurance, and have additional medium term product and service plans.

We have a full service banking operation in Northern Ireland serving both retail and business customers. Our branch network has been restructured and upgraded in 2013 and we are keen to develop this business further. Our financial performance has improved but further improvement is required. Our separate car finance subsidiary operating under NIIB and Northridge brands, based in Northern Ireland but addressing the whole UK market, has had another good year and we see potential for it to develop further.

During 2013 we announced that our existing business banking operations in GB would close for new business. Our future focus in GB will very much be consumer orientated recognising that, in addition to our relationship with the Post Office, we also have a significant, high quality residential mortgage portfolio generated under Bank of Ireland and Bristol & West brands.

In addition to improvements in profitability and operating efficiency, we have also strengthened our capital position and have thereby become a stronger bank better able to serve our customers. Whilst we have been operating in a difficult market over the last three years, we have not overlooked the importance of sustaining and developing our customer relationships. We appreciate that many of our customers have also had their own challenging experiences to deal with over this period, and where this has been the case we have sought to be supportive. Looking ahead, we are committed to high standards of conduct in our engagement with our customers and we thank them for their business.

These have been demanding times for our people, and the Board would like to express its appreciation for the commitment, effort and professionalism of our employees. Much has been achieved and we look to the future with increasing confidence.



Christopher Fisher
5 March 2014

Strategic Report

The directors present their Strategic Report for the year ended 31 December 2013.

Key Performance Measures

Performance summary	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Group operating profit before impairment charges on financial assets	**148**	**21**
Impairment charges on financial assets	(125)	(183)
Share of profit after tax of jointly controlled entity	34	32
Profit / (loss) before taxation	**57**	**(130)**
Group performance measures		
Net interest margin %	1.70%	1.07%
Average interest earning assets	24,482	24,626
Cost income ratio %	65%	93%
Segmental operating profit before impairment charges on financial assets[1]		
Great Britain (GB) Consumer Banking	169	74
Northern Ireland (NI)	25	12
Great Britain (GB) Business Banking	11	14
Other	(57)	(79)
Total operating profit before impairment charges on financial assets	**148**	**21**
Impairment charges on loans and advances to customers		
Residential mortgages	(8)	(14)
Non-property SME and corporate	(34)	(29)
Property and construction	(69)	(122)
Consumer	(14)	(18)
Total impairment charges on financial assets	**(125)**	**(183)**

Consolidated balance sheet and key metrics	31 December 2013 £m	31 December 2012 £m
Equity attributable to owners of the Parent	1,533	1,354
Total assets	35,895	52,346
Loans and advances to customers (after impairment provisions)	17,928	18,018
Customer accounts	20,857	23,275
Loan to deposit ratio %	86%	77%
Capital (Basel II basis)		
Core tier 1 capital ratio %	11.0%	8.9%
Total tier 1 capital ratio %	13.4%	10.8%
Total capital ratio %	20.3%	16.7%
Risk weighted assets (RWA)	10,618	11,314

Definition of Key Performance Measures

Net interest margin – is defined as net interest income for the year ended 31 December, compared to twelve months average interest earning assets.

Average Interest Earning Assets – is defined as the twelve months average of the total customer loan balances, cash placements, securities balances and net balances owed by the Parent (The Governor and Company of the Bank of Ireland).

Cost income ratio – is defined as operating expenses compared to total operating income.

Loan to deposit ratio – is defined as loans and advances to customers as at 31 December compared to customer deposits as at 31 December, after excluding related party balances.

Capital ratios – capital ratios express the Group's capital as a percentage of its risk weighted assets as defined by the UK Prudential Regulation Authority (PRA). These ratios are published consistently by the banking industry in the UK.

[1] *Operating segments are defined on page 91.*

1.1 Purpose of the Strategic Report

The Strategic Report is a new statutory requirement under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013, replacing the previous Operating and Financial Review, and is intended to be fair and balanced, and to provide information that enables the Directors to be satisfied that they have complied with Section172 of the Companies Act 2006 (which sets out the Directors' duty to promote the success of the company).

The strategic report has been presented on a consolidated basis for the years ended 31 December 2013 and 31 December 2012.

Percentages throughout the document are calculated on the absolute underlying figures and so may differ from the variances calculated on the rounded numbers presented.

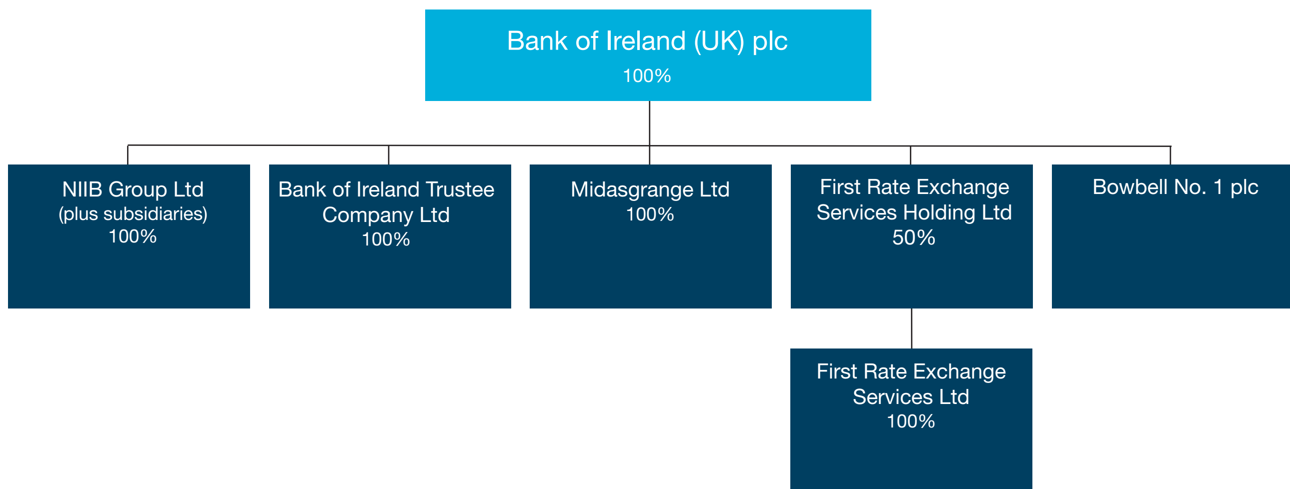
1.2 Group Structure

At 31 December 2013, the Group consisted of the Bank and its share of the following entities:

- 100% of NIIB Group Limited (NIIB) – a car finance and consumer lending group;
- 50% of First Rate Exchange Services Holdings Limited (FRESH), a joint venture, which, via its wholly owned subsidiary, First Rate Exchange Services Limited (FRES), is a wholesale and retail provider of foreign exchange with retail distribution primarily via Post Office;
- 100% of Bank of Ireland Trustee Company Limited – a multi-restricted intermediary providing advice to clients on financial services products operating in the Northern Ireland market;
- 100% of Midasgrange Limited – this company traded as Post Office Financial Services until 3 September 2012 when the trade and assets transferred to the Bank; and
- Bowbell No. 1 plc (Bowbell) - a special purpose entity which acquires mortgage loans and issues mortgage backed securities. The Bank does not own more than half of the voting power in the company but it is deemed a subsidiary in accordance with SIC 12.

The Group's immediate and ultimate parent is The Governor and Company of the Bank of Ireland ('the Parent').

The Bank is a public limited company domiciled in the UK.



1.3 UK Economic and Market Environment

The UK is the Group's primary market.

The improvements in the UK operating and financial environment experienced during 2013 are expected to continue into 2014.

The UK economic recovery gathered momentum in 2013, prompting a series of positive revisions to growth forecasts as the year progressed. For example, 2013 and 2014 GDP forecasts were upgraded to 1.4% (0.9%) and 1.9% (1.5%) respectively[1], consistent with the more favourable sentiment confirmed by the various Market / CIPS Purchasing Manager (PMI) surveys for manufacturing, construction and services, all of which recorded multi-year highs.

The downside risks to the UK from external markets appeared to recede during the year as the euro-area emerged tentatively from an 18 month recession while US legislators reached a short-term compromise, averting a potential debt default. As a further sign of stability and improved confidence, it was noted that the perceived probability of a high impact event in the UK financial system had fallen to its lowest level since the survey was introduced in 2008[2].

The UK's labour market continued to improve at a steady pace during 2013. The jobless rate declined to 7.2% in the 3 months to December 2013 bringing total employment back above its pre-recession peak. However, pay growth remained very subdued with average earnings (excluding bonuses) rising 1% year on year to December 2013[3]. With Consumer Price Inflation (CPI) inflation consistently above the 2.0% target during 2013, the squeeze on household incomes and spending power continued[3].

The Bank of England continued to temper speculation of early interest rate increases by highlighting the availability of macroprudential tools of monetary policy while also emphasising the jobless rate as a necessary but not sufficient condition for rate decisions.

A decline in the annual rate of CPI to 2.0% in December 2013 was also supportive of the 'no change' interest rate policy continuing into 2014 at least.

In the year to December, the average UK house price growth accelerated to 8.4%, with growth in all regions. The London and South-East markets again set the pace, in part a reflection of supply constraints, while in Northern Ireland there were further signs of market stabilisation and some recovery in sales volumes[4].

While still well below pre-crisis peaks and long-run historic averages, trends in the UK mortgage market were supportive of more favourable housing conditions during 2013.

In December 2013, the 2013 estimate for Gross Mortgage Advances were revised up to £176 billion from £145 billion previously representing year on year growth of 21% while also forecasting a further increase to £195 billion in 2014[5].

The accelerated introduction of the Help to Buy guarantee initiative is expected to provide an additional stimulus to transaction levels against the backdrop of falling unemployment and rising confidence.

The firmer trends in the UK commercial property market were evident during the year with a modest rise in capital values across all sectors and with some signs that growth was no longer restricted to prime locations in London with the more favourable economic climate enabling stronger performances in selected regional markets. During 2013 the capital values rose overall by 3.8%, with the pace of recovery accelerating in the final few months of the year[6].

By the end of 2013, the policymakers on the Bank of England's Monetary Policy Committee had confirmed a 'sustained recovery' during H2 while simultaneously indicating no urgency to raise interest rates.

[1] The International Monetary Fund (IMF), Autumn outlook.
[2] Bank of England biannual System Risk Survey, November 2013.
[3] Office for National Statistics.
[4] Nationwide.
[5] Council for Mortgage Lenders.
[6] Investment Property Databank, UK Monthly Property Index, December 2013.

1.4 Our business strategy and goals

The Group is a UK retail focused bank committed to long term relationships with customers and strategic partners.

The overall goal of the Group is to be a leading provider of flexible, accessible financial services and products to UK customers both directly and via the partnership with the Post Office.

In support of this strategy the Group leverages the overall scale and capability of the Parent.

The strategies at segment level are set out below.

GB consumer banking
The partnership with the Post Office is the core component of the Group's consumer banking strategy in GB. The Post Office is customer focused, has a trusted brand and an unrivalled branch network.

The Group is the primary provider of financial services to the Post Office providing a comprehensive range of savings, lending, payment and insurance products under a contract that was extended in 2012 and now covers the period until 2023.

The Group and the Post Office have worked together successfully in 2013 to increase the product range and access options for the customer. This includes the launch on a trial basis in May 2013 of a Post Office current account in the East Anglia region and the recruitment, by the Post Office, of a team of mortgage advisers to provide customers with the ability to obtain a mortgage at selected Post Office branches, in addition to existing telephone and online access options.

The Group joined the UK Government's Help to Buy scheme in early December 2013 in order to increase the range of mortgage options available to First Time Buyers via the Post Office.

In addition during 2013 the Post Office has invested in the modernisation of its network and has increased opening hours for customers.

FRES, the Group's joint venture with the Post Office, has maintained its position as the leading provider of retail foreign currency in the UK and has expanded its product range to meet changes in customer demand.

The Group also supplies ATM services to the Post Office with over 2,000 machines in operation at December 2013 and identified potential for further growth.

The shared strategy of the Group and the Post Office is to achieve further growth through a combination of continuing to increase awareness of the Post Office as a destination for financial services, providing easy access to a full range of simple, transparent, value for money products, and building on the existing financial services relationships already in place, with over 2.7 million customers.

In addition to funding lending through the partnership with the Post Office, savings balances raised under the Post Office brand also support the funding of other UK lending, including residential mortgages originated under Bank of Ireland and Bristol & West brands, as well as consumer lending (primarily car finance) provided under NIIB and Northridge brands.

During 2013 the Group acquired a further £1.46 billion of UK residential mortgages from the Parent at a fair value of £1.31 billion, building on previous acquisitions in 2012 thereby improving balance sheet and liquidity efficiency. The Group continues to maintain a sufficient liquidity and capital position to enable further mortgage acquisitions in 2014.

NIIB delivered profitability of £22 million for year ended 31 December 2013, reflecting loan book growth of 8.2% and continued low bad debt levels. NIIB's strategy is to continue to develop its relationships with large car dealer groups and other introducers across the UK, building on its strong positions in the Scottish and Northern Ireland markets and increasing its market share in England.

Northern Ireland (NI)
The NI business offers a full range of banking products for retail and SME customers, with a strong focus on providing personal and business customers with advice, sales and support.

The NI business reported a net loss (after impairment charges) for 2013 of £50 million, compared to a net loss for 2012 of £112 million. The NI Business is currently undertaking a series of initiatives in order to progress to a period of renewed profitability. These initiatives are progressing in line with expectations.

During the year the Group reaffirmed its business strategy in Northern Ireland to support the region's economic growth and to provide competitively-priced products and services to retail and business customers. To help deliver this strategy, the Group undertook a review of all customer channels in Northern Ireland, including its branch network, to ensure it was cost-effective and fit for purpose. As part of this review the Group closed nine smaller branches, where the volume of business was insufficient to sustain them, but also invested in upgrading and modernising all thirty-five remaining branches. The Group's priority remains focused on ensuring its branch network and direct channels are fully integrated while also maintaining a significant geographical spread across Northern Ireland.

The Group in Northern Ireland also recognises the importance of promoting SMEs as one of the key drivers for economic recovery and as such another key element of the Group's support to SMEs is the Enterprise Programme. The Enterprise Programme is an ongoing series of business events that are hosted throughout the year, including an Enterprise Week in May and November. It was developed to help support SMEs in their own communities.

1.4 Our business strategy and goals (continued)

Business Banking GB
The Group's business banking activities in GB have faced challenges in recent years given the high capital requirements attaching to commercial lending and the challenging economic environment.

The strategy for the business is a managed deleverage of the loan book over the medium term. This strategy is consistent with the amendments to the EU Restructuring Plan agreed between the Parent and the EU which were announced on 9th July 2013. Under the amended EU Restructuring Plan, the Parent committed that it would exit from its GB based business banking and corporate banking businesses.

During 2013, GB business banking volumes reduced in the Group by £0.5 billion, with comparable volumes of deleveraging anticipated in 2014.

This strategy does not impact on the Group's consumer banking businesses in Great Britain including its partnership with the Post Office, or its activities in Northern Ireland.

Capital and liquidity
The Group was fully compliant with its regulatory capital and liquidity requirements throughout 2013.

The Group incurred losses in 2012 driven by a combination of increased funding costs and high impairment charges and, whilst it has returned to profitability in 2013, profit levels still need to recover further and achieve the required cost of capital (with cost in this respect being the medium term return that the Parent and its external shareholders require on existing or new capital).

During the year the Group increased the customer interest rate on a portfolio of UK residential mortgages where the customer rate was insufficient to meet its funding costs and provide a return on capital requirements. Whilst the Group fully recognises the potential impacts on customers when rates are increased, it considers that these actions were necessary to support the medium and longer term viability of the Group and are consistent with the terms and conditions agreed and in place between the customers and the Group.

The Group's strategy is to seek new lending and other business opportunities that are aligned with its risk appetite and that will deliver a sufficient rate of return on capital.

The introduction with effect from 1 January 2014 of the Capital Requirements Regulation (CRR/Basel III as published in the Official Journal of the EU on 27 June 2013) increases the regulatory capital requirements of the Group. This primarily results in certain balance sheet items, including deferred tax asset balances, which are now required to be deducted directly from regulatory capital.

Based on the latest guidance, the Group is fully compliant with the aforementioned increased regulatory capital requirements at 1 January 2014.

At 31 December 2013 the Group had a total capital ratio of 20.3% and a core tier 1 capital ratio of 11.0% (Basel II basis).

At the end of 2012 the customer deposit balances held by the Group were well in excess of the level required to support compliance with the Group's risk appetite requirements and its regulatory liquidity obligations.

Customer deposit balances have been reduced by £2.4 billion during 2013 in order to reduce this excess. At the end of 2013 the Group retains a strong liquidity position fully compliant with risk appetite and regulatory obligations and with customer deposits in excess of customer lending with a loan to deposit ratio of 86%.

The Group's present liquidity strategy is to remain primarily customer deposit funded with no material reliance on wholesale or Central Bank funding.

The introduction of Basel III will also result in changes to regulatory liquidity requirements including the introduction of new measures such as the Liquidity Coverage Ratio and the Net Stable Funding Ratio. The Group actively monitors its liquidity position under these new ratios and requirements and takes them into account in the creation, execution and review of its funding plans.

Customer and compliance strategy
The formal separation of the former Financial Services Authority (FSA) into the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) on 1 April 2013 has resulted in an increased focus on 'conduct' or customer risk. It has always been important for the Group to ensure that its customers and the way it relates to them are a key consideration in how it does business. The Group is responding to the challenge laid down by the FCA to the industry by undertaking a wide ranging review of how it manages and mitigates the risks to customers that arise in its activities to ensure a continuing pro-active and customer centric approach in all aspects of its product and distribution activities. The Group has been participating in the FCA thematic review of complaint management and it regards this as an opportunity to ensure that it continues to enhance how it responds to customers when issues arise. The Group currently has a very low level of referrals to the Ombudsman by customers not happy with the outcome of any complaint and an Ombudsman complaint 'overturn' rate that is less than half of the industry average. The Group wants to build on that position to ensure that, when issues arise, it deals with them both quickly and effectively to ensure a positive outcome for customers.

1.5 Summary of Group developments during 2013

During 2013 the following Group developments took place:

- the Group acquired a number of mortgage portfolios from the Parent with a total loan value of £1.46 billion for a fair value of £1.31 billion, representing a weighted average price of 90%. Included within the adjustment for fair value were both expected credit losses and the differential between the customer interest rates on the assets and current market interest rates for similar assets;
- the Parent invested additional capital of £35 million in support of the mortgage acquisitions detailed above;
- In December 2013, the Group commenced the process of replacing its gross flow cash hedging approach (by repaying inter-group borrowings and placings) and replacing it with a derivative hedging model for managing interest rate risk. Derivatives are executed with the Parent only and are subject to an ISDA[1] and CSA[2] and therefore daily collateral requirements are calculated and posted as required;
- the Group changed its transfer pricing methodology during the year, with the development of the an internal transfer pricing process, based on its own retail deposit funding costs rather than the funding cost of the Parent. (Refer to note 33 for further information);
- In December 2013, the Parent transferred £86 million of historic taxation losses to the Group in respect of transferred activities that are now carried on within the Group. The £86 million transfer was accounted for as a capital contribution;
- the Group became a member of the Sterling Monetary framework (SMF) in February 2013 and subsequently a member of the Funding for Lending Scheme (FLS). £250 million was drawn down via FLS in June 2013 and repaid in January 2014;
- the Group joined the UK Government's Help to Buy Scheme in early December 2013;
- In December 2013 the EU Commission, as part of the Parent's revised restructuring plan, agreed that the Group could move to a managed deleverage of its GB Business Banking portfolio; and
- the Group announced the closure of new business referrals to Bank of Ireland Trustee Company Limited in November 2013, with plans to close the operation by early 2014.

[1] ISDA - International Swaps and Derivatives Association Master Agreement
[2] CSA - Credit Support Annex

1.6 Financial Review

1.6.1 Trading Performance

Summary Group consolidated income statement	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m	Change %
Net interest income	415	263	58%
Net fee and commission income	6	35	(83%)
Net trading income	-	2	(100%)
Other operating income	1	(7)	114%
Total operating income	**422**	**293**	44%
Operating expenses	(274)	(272)	1%
Operating profit before impairment charges on financial assets	**148**	**21**	**605%**
Impairment charges on financial assets	(125)	(183)	32%
Share of profit after tax of jointly controlled entity	34	32	6%
Profit / (loss) before taxation	**57**	**(130)**	**144%**
Taxation credit	4	38	(89%)
Profit / (loss) for the year	**61**	**(92)**	**166%**

1.6.2 Net Interest Income

Net interest income / Net interest margin	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Net interest income	415	263
Average interest earning assets	24,482	24,626
Net interest margin %	1.70%	1.07%

Net interest income for the year ended 31 December 2013 was £415 million compared to £263 million for the year ended 31 December 2012. Gross interest income was £1,101 million (2012: £1,305 million) and consists principally of interest earned on customer lending and on amounts placed with the Parent. Interest expense is £686 million (2012: £1,042 million) and represents interest paid or payable on customer deposits and on amounts borrowed from the Parent.

The net interest margin for the year ended 31 December 2013 was 1.70% compared to 1.07% for the year ended 31 December 2012, representing an increase of 63 basis points. This reflects repricing of both assets and liabilities and more efficient balance sheet management, through reduction of the liquid asset portfolio, partly offset by lower funding income allocated from the Parent.

1.6.3 Net Fee and Commission Income

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Fee and commission income		
- ATM service fees	59	58
- Insurance commissions	7	32
- Banking fees and other commissions	28	29
- Foreign exchange and credit card	19	21
- Other	5	2
Fee and commission expense	(112)	(107)
Net fee and commission income	**6**	**35**

The Group's net fee and commission income for the year ended 31 December 2013 was £6 million compared to £35 million for the year ended 31 December 2012. This year on year reduction of £29 million was driven by commission expense increases, primarily due to higher commission payments following the extension and strengthening of the financial services relationship with the UK Post Office in the second half of 2012.

Note: Changes to the structure of the Group's contracts with their insurance providers during 2012 and 2013 has resulted in changes in the presentation of various line items within net fee and commission income. This has resulted in lower insurance commissions reported in 2013 compared to 2012, with correspondingly lower insurance fees and commissions expense year on year.

1.6.4 Operating Expenses

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Staff costs	27	21
Other costs	247	251
Operating expenses	**274**	**272**

The majority of the Group's cost base is from outsourced services, being the costs of distribution, product manufacture and support provided by the Parent. The year on year increase in staff costs is a result of the annualised impact of the transfer from the Parent of a number of key staff involved in distribution, product provision and risk management activities in October 2012. Refer to note 7 for more details. Other costs have reduced year on year reflecting reduced regulatory and professional costs and ongoing cost initiatives across the NI and GB businesses, offset somewhat by costs associated with change initiatives. Included within other costs are £17 million in charges relating to the Financial Services Compensation Scheme (FSCS) levy (year ended 31 December 2012: £24 million).

1.6.5 Impairment Charges on Loans and Advances to Customers

Impairment charges on loans and advances to customers	**Year ended 31 December 2013 £m**	Year ended 31 December 2012 £m
Residential mortgages	8	14
Non-property SME and corporate	34	29
Property and construction	69	122
Consumer	14	18
Total impairment charges on loans and advances to customers	**125**	**183**
Impairment charge basis points	**32 bps**	**109 bps**

The impairment charge for the year ended 31 December 2013 on loans and advances to customers was £125 million, compared to £183 million for the year ended 31 December 2012. The charge comprises £103 million in respect of commercial lending, £14 million in respect of consumer credit card lending and £8 million in respect of residential mortgages.

Non property, SME and corporate impairment charges increased by £5 million year on year with trading conditions remaining difficult. Property and construction impairment charges improved by £53 million, with some signs of improving conditions.

The future trend in impairments remains significantly dependent on economic conditions, with our commercial lending portfolio's performance directly impacted by the challenging commercial property market conditions, particularly in Northern Ireland. Refer to pages 33 to 37 in the Risk management section for further credit risk details in relation to loans and advances to customers.

1.6.6 Taxation Credit

The taxation credit for the Group was £4 million for the year ended 31 December 2013 compared to a taxation credit of £38 million for the year ended 31 December 2012.

Excluding the £34 million (year ended 31 December 2012: £32 million) income from our jointly controlled entity, FRESH, the effective tax rate for the year ended 31 December 2013 was 17% (year ended 31 December 2012: 23%).

The effective tax rate is influenced by a number of factors including the fair value unwind on acquired mortgages not being taxable within the Group and the impact on deferred tax of the reduction in the UK corporation tax rate to 20% with effect from 1 April 2015.

1.6.7 Summary Consolidated Balance Sheet

	31 December 2013 £m	31 December 2012 £m	Change %
Cash and balances with Central Banks	4,125	6,380	(35%)
Loans and advances to banks[1]	12,824	27,090	(53%)
Loans and advances to customers	17,928	18,018	-
Available for sale financial assets	482	341	41%
Total other assets	536	517	4%
Total assets	**35,895**	**52,346**	**(31%)**
Deposits from banks[2]	11,660	25,742	(55%)
Customer accounts	20,857	23,275	(10%)
Subordinated liabilities	658	658	-
Total other liabilities	1,187	1,317	(10%)
Total liabilities	**34,362**	**50,992**	**(33%)**
Equity attributable to owners of the Parent	1,533	1,354	13%
Total equity and liabilities	**35,895**	**52,346**	**(31%)**
Loan to deposit ratio	**86%**	**77%**	**9%**

[1] Included within loans and advances to banks is a balance due from the Parent of £11,646 million (31 December 2012: £25,885 million) and £1,178 million (31 December 2012: £1,205 million) due from external bank counterparties. Refer to note 14.

[2] Included within deposits from banks is a balance due to the Parent of £11,651 million (31 December 2012: £25,737 million) and £9 million (31 December 2012: £5 million) due to external bank counterparties. Refer to note 21.

1.6.8 Loans and Advances to Banks and Deposits from Banks

In December 2013, the Group commenced the process of replacing its gross flow cash hedging approach. This involved settling inter-group borrowings and placings and replacing these with a derivative hedging model for managing interest rate risk. Prior to that date, the Group had used a gross flow cash hedging model to manage interest rate risk with the Parent, whereby customer loans were hedged with a loan from the Parent and customer deposits were hedged by placing a deposit with the Parent. As a result, the Group had balances with the Parent on both sides of its balance sheet, which were disclosed within loans and advances to banks and deposits from banks. The impact of the aforementioned change in hedging approach has been to reduce the total assets and total liabilities on the Group's balance sheet by £12.3 billion, thereby optimising liquidity positions and improving the Group's leverage ratio. Over time, the gross flow cash hedging deals with the Parent will be replaced by derivative contracts, with the Parent.

1.6.9 Loans and Advances to Customers

Composition by portfolio - loans and advances to customers	31 December 2013 £m	31 December 2013 % of Book	31 December 2012 £m	31 December 2012 % of Book
Residential mortgages	13,078	70%	12,568	67%
Non-property SME and corporates	2,016	11%	1,980	11%
Property and construction	2,455	13%	3,074	16%
Consumer	1,098	6%	1,091	6%
Loans and advances to customers (before impairment provisions)	**18,647**	**100%**	**18,713**	**100%**
Impairment provisions	(719)		(695)	
Loans and advances to customers (after impairment provisions)	**17,928**		**18,018**	

Gross loans and advances to customers of £18.6 billion have reduced by £0.1 billion in the year. The key drivers of the move are as follows:

- the Group acquired a number of mortgage portfolios from the Parent with a total loan value of £1.46 billion for consideration of £1.31 billion, representing a weighted average price of 90%. Included within the discount were both expected credit losses and the differential between the customer interest rates on the assets and current market interest rates for similar assets;
- excluding the aforementioned mortgage acquisitions other mortgage lending reduced by a net £0.8 billion. This reflected £0.9 billion of new loans through the Post Office and NI which were more than offset by repayments on the overall mortgage portfolio;
- a net reduction in the commercial lending portfolio of £0.6 billion (12%). Of this reduction £0.5 billion relates to GB business banking volumes, which are deleveraging over the medium term. Demand for commercial lending in Northern Ireland remains subdued; and
- consumer lending, Bank of Ireland and Post Office branded credit card lending and NIIB Group lending to UK customers was largely unchanged year on year with NIIB business growth of £86 million offset by reductions primarily in Bank of Ireland consumer lending.

Specific provisions increased by 4% to £635 million at 31 December 2013, from £613 million at 31 December 2012 due primarily to movement in the commercial land and development portfolio. Incurred but not reported provisions increased by 2% to £84 million at 31 December 2013, from £82 million at 31 December 2012.

1.6.10 Liquid Assets

Liquid assets	31 December 2013 £m	31 December 2012 £m
Balances with Central Banks	4,088	6,350
Available for sale financial assets	482	341
Interbank placements	150	416
Total	**4,720**	**7,107**

The liquid assets portfolio comprises Bank of England deposits, available for sale assets and bank placements, which can be used to raise liquidity, either by sale, or through secured funding transactions. This portfolio of £4.7 billion decreased by £2.4 billion during 2013, reflecting the Group's strategy of efficiently managing its balance sheet.

At 31 December 2013 the liquid asset portfolio primarily comprises £4.1 billion of Bank of England deposits, £339 million with multi-lateral development banks, £98 million of UK government treasury bills, £45 million of Finnish government paper, and £150 million placed with the Parent. Placements with the Parent are included in loans and advances to banks and while they are considered liquid assets by the Group they are not PRA BIPRU eligible liquid assets.

The Group has remained in full compliance with the regulatory liquidity regime in the UK throughout 2013, and as at 31 December 2013 maintains a buffer significantly in excess of regulatory liquidity requirements.

The liquid assets presented above do not include cash or general bank accounts that are utilised in the day to day operations of the Group.

1.6.11 Customer Accounts

Customer accounts	31 December 2013 £m	31 December 2012 £m
BoI branded deposits	2,112	2,395
BoI branded current accounts	2,521	2,324
Post Office branded deposits	16,224	18,556
Total	**20,857**	**23,275**

The Group has a mix of retail and non-retail deposits and current accounts, under both Bank of Ireland and Post Office brands. As at 31 December 2013, the constituent components of customer accounts were retail deposits and current accounts of £18 billion, compared to £21 billion at 31 December 2012, and non-retail of £2.8 billion compared to £2.3 billion at December 2012.

Of the retail deposits, £16.2 billion of these related to Post Office branded deposits, which have decreased by £2.3 billion (13%) over the year reflecting the Group's balance sheet requirements.

1.6.12 Funding

The Group's funding position remains strong at 31 December 2013, with a loan to deposit ratio of 86% (31 December 2012: 77%). The increase in loan to deposit ratio primarily reflects the net effect of stable year on year loans and advances to customers, offset by the impact of lower volumes of deposits.

The Group currently does not rely on wholesale funding to fund core activities, however it maintains the operational flexibility to borrow from the market and from other banks including, but not restricted to, the Parent.

In December 2013 the PRA issued guidance on the UK implementation of the Capital Requirements Directive IV (CRD IV). Presently the Group calculates a Liquidity Coverage Ratio (LCR) and a Net Stable Funding Ratio (NSFR) based on the current draft EBA guidelines and continues to anticipate buffers above the required levels of 100% at 31 December 2013.

1.6.13 Regulatory Capital (Basel II)

Composition of regulatory capital	31 December 2013 £m	31 December 2012 £m
Tier 1		
Ordinary share capital	851	816
Capital contributions	386	300
Retained earnings and other reserves	(72)	(111)
Core tier 1 capital	**1,165**	**1,005**
Non-cumulative callable preference shares	300	300
Total tier 1 capital before regulatory adjustments	**1,465**	**1,305**
Regulatory adjustments		
Intangible Assets	(46)	(52)
Non-qualifying investments	(1)	(34)
Total tier 1 capital after regulatory adjustments	**1,418**	**1,219**
Tier 2		
Dated loan capital	658	658
Regulatory adjustments		
Non-qualifying investments	(1)	(34)
Disallowable Tier 2 capital	-	(31)
IBNR impairment provisions	**82**	**73**
Total tier 2 capital after regulatory adjustments	**739**	**666**
Total regulatory capital	**2,157**	**1,885**

Capital ratios	31 December 2013	31 December 2012
Core tier 1 ratio	11.0%	8.9%
Tier 1 ratio	13.4%	10.8%
Total capital ratio	20.3%	16.7%

Capital figures disclosed reflect the consolidated UK regulatory position for the BoIUK regulatory group which consists of the Bank and NIIB Group only.

The Group is strongly capitalised and at 31 December 2013 had a total capital ratio of 20.3%. During the year, the Group issued £35 million of additional share capital and received £86 million by means of a capital contribution in respect of historic taxation losses transferred from the Parent. The Group continues to have an active approach to capital management, the focus of which is to ensure adequate capital to support future business plans.

1.6.13 Regulatory Capital (Basel II) (continued)

Risk-weighted Assets	31 December 2013 £m	31 December 2012 £m
RWAs by risk type		
Credit Risk	9,986	10,778
Operational, Market and Counterparty Credit Risk	632	536
	10,618	**11,314**
RWAs by businesses	**£m**	£m
Commercial lending	3,841	4,623
Mortgages	4,873	4,891
NIIB	693	638
Credit Cards	267	274
Other	944	888
	10,618	**11,314**

Capital requirements for calculating RWAs	Capital required £m	RWA £m	Exposure £m
Central Governments or Central Banks	-	-	5,306
Multinational Development Banks	-	-	340
Corporates	231	2,889	2,885
Retail	77	964	1,304
Secured by mortgages on residential property	377	4,713	12,990
Past due items	89	1,113	1,493
Short term claims on institutions and corporates	5	64	291
Other items	20	243	439
Credit risk	**799**	**9,986**	**25,048**
Operational, Market and Counterparty Credit Risk	**50**	**632**	**-**
Total	**849**	**10,618**	**25,048**

Movement in total regulatory capital	31 December 2013 £m	31 December 2012 £m
Opening core tier 1 capital	**1,005**	**1,022**
Ordinary shares issued	35	60
Capital contribution	86	-
Contribution to core tier 1 capital from profit / (loss)	39	(77)
Closing core tier 1 capital	**1,165**	**1,005**
Opening other tier 1 capital	**214**	**196**
Other, including regulatory adjustments	39	18
Closing other tier 1 capital	**253**	**214**
Opening tier 2 capital	**666**	**523**
Subordinated debt issued	-	135
Other, including regulatory adjustments	73	8
Closing tier 2 capital	**739**	**666**
Closing total regulatory capital	**2,157**	**1,885**

1.6.14 Regulatory Capital (Basel III)

Composition of regulatory capital

Basel II 31 December 2012	Basel II 31 December 2013		Pro forma Basel III transitional 1 January 2014	Pro forma Basel III fully loaded 31 December 2013
		Capital Base		
1,005	1,165	Total Equity	1,165	1,515
-	-	Regulatory Deductions	(176)	(176)
1,005	**1,165**	**Core tier 1 / Common equity tier**	**989**	**1,339**
		Additional Tier 1		
300	300	Preference Shares / Other AT1 compliant instruments	300	200
(86)	(47)	Regulatory Deductions	(60)	-
1,219	**1,418**	**Total tier 1 capital**	**1,229**	**1,539**
		Tier 2		
658	658	Dated loan capital	658	350
8	81	Regulatory Add ons net of deductions	142	82
666	**739**	**Total tier 2 capital**	**800**	**432**
1,885	**2,157**	**Total regulatory capital**	**2,029**	**1,971**

Capital ratios

Basel II 31 December 2012	Basel II 31 December 2013		Pro forma Basel III transitional 1 January 2014	Pro forma Basel III fully loaded 31 December 2013
8.9%	11.0%	Core tier 1 / Core Equity Tier 1 ratio	9.7%	13.1%
10.8%	13.4%	Total Tier 1 ratio	12.0%	15.1%
16.7%	20.3%	Total capital ratio	19.9%	19.3%

Risk-weighted Assets (RWAs)

Basel II 31 December 2012	Basel II 31 December 2013		Pro forma Basel III transitional 1 January 2014	Pro forma Basel III fully loaded 31 December 2013
10,778	9,986	Credit Risk	9,605	9,605
536	632	Operational, Market and Counterparty Credit Risk	614	614
11,314	**10,618**	**RWAs by risk type**	**10,219**	**10,219**

1.6.14 Regulatory Capital (Basel III) (continued)

Basel III

The Capital Requirements Directive (CRD IV) and the Capital Requirements Regulation (CRR) were published in the Official Journal of the EU on 27 June 2013. The CRR had direct effect in EU member states and CRD IV was required to be implemented through national legislation in EU member states by 31 December 2013. CRD IV also includes requirements for regulatory and technical standards to be published by the European Banking Authority (EBA). Many of these have not yet been published or their impact is uncertain. The CRD IV legislation will be implemented on a phased basis from 1 January 2014, with full implementation by 2019.

The Basel III / CRD IV transition rules result in a number of new deductions from CET 1 capital. In December 2013, the PRA issued guidance on the transitional implementation of CRD IV which directed UK banks that CET1 capital deductions would be applied at 100% from 1 January 2014.

The pro forma ratios as outlined in the above table represent estimates reflecting the Group's interpretation of the CRD IV rules as published on 27 June 2013. The actual capital ratios under CRD IV may differ as the rules are assessed in their entirety, related technical standards are finalised and other guidance is issued by the relevant regulatory bodies.

Basel III pro forma Transitional Ratio at 1 January 2014

Risk Weighted Assets (RWA) at 1 January 2014 of £10.2 billion compares to Basel II RWA at 31 December 2013 of £10.6 billion.

The Common equity tier 1 (CET 1) pro forma ratio at 1 January 2014 of 9.7% compares to the Basel II Core tier 1 ratio of 11.0% at 31 December 2013. The decrease primarily relates to 100% deduction from CET1 of DTA's relating to future profitability and temporary differences.

The total capital pro forma ratio at 1 January 2014 of 19.9% compares to the Basel II total capital ratio of 20.3% at 31 December 2013 primarily driven by the decline in CET1 capital as outlined above.

Basel III pro forma Fully Loaded Ratio

The Group's pro forma CET 1 ratio, is estimated at 13.1% as at 31 December 2013 on a fully loaded basis. The Group's pro forma ratio excluding the projected capital restructure is estimated to be 9.7% at 31 December 2013.

The Group expects to remain above the Basel Committee indicated minimum level leverage ratio of 3% on a transitional basis and on a fully loaded pro forma basis. The leverage ratio is above 3% at 31 December 2013.

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

1.6.15 Segmental Performance

Consolidated income statement - profit / (loss) before taxation	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m	Change %
Great Britain (GB) Consumer Banking	185	77	140%
Northern Ireland (NI)	(50)	(112)	55%
Great Britain (GB) Business Banking	(21)	(16)	(31%)
Other	(57)	(79)	28%
Profit / (loss) before taxation	**57**	**(130)**	**144%**

The results of the Group can be summarised by segment as follows:

Great Britain (GB) Consumer Banking – the business offers a wide range of products under the Bank of Ireland, Post Office, Bristol & West and NIIB brands. The Post Office product proposition includes deposits, mortgages, personal loans, credit cards, insurance and foreign exchange through the Group's jointly controlled entity under FRES.

Consumer banking profits year on year increased from £77 million to £185 million reflecting a recovery in deposit margins and an improved performance in consumer lending products including Bank of Ireland and Post Office mortgages, and NIIB car finance.

The aforementioned improvement in consumer lending performance in 2013 resulted from growth in the Post Office branded mortgages combined with further acquisitions of residential mortgage assets from the Parent over the year. Lending margins continued to improve on the Bank of Ireland and Bristol & West mortgage portfolios, after repricing initiatives in 2012 and 2013.

Consumer deposit margin performance reflected the impact of strong deposit retention on both Post Office and Bank of Ireland branded deposits, and lower customer pay rates across the industry.

The mortgage assets acquired from the Parent in 2013 had a loan value of £1.46 billion with a fair value of £1.31 billion, representing a weighted average price of 90%.

Total assets acquired from the Parent in 2012 and 2013 totalled £4.9 billion as at 31 December 2013 and include a cumulative credit risk adjustment of £42 million. This credit risk adjustment comprises anticipated losses over the remaining life of the loans. Incurred losses on this portfolio at 31 December 2013 totalled £3.2 million.

Refer to page 75 for further details of the Group's accounting policy on financial assets.

Northern Ireland (NI) – the NI business includes the results of the Bank of Ireland branded branch network and business centres, together with the credit card, mortgage portfolio and banknote issuing activity in Northern Ireland. The performance has improved year on year reflecting a 15% increase in total income combined with a 40% reduction in impairment losses. Demand for new lending remained low in 2013, but the Group remains committed to supporting its operations in this market.

Great Britain (GB) Business Banking – the business includes £1.7 billion of commercial lending and £0.9 billion of retail deposits; with losses for the year totalling £21 million, increasing from £16 million in 2012. The reduction in year on year performance is driven primarily by reduced lending income reflecting the ongoing deleveraging in the loan portfolio offset somewhat by reduced costs.

Other – the Group’s funding, liquidity and capital position are managed centrally and the related costs are held in this segment together with the cost of central risk and control functions and regulatory related costs including the FSCS levy of £17 million (2012: £24 million). The net loss reported within this segment decreased in 2013 due to lower liquid asset holdings and net funding costs, arising from a more efficient balance sheet structure and an improved loan to deposit ratio.

1.7 Principal Risks and Uncertainties

The table below outlines a summary description of the principal risks and uncertainties faced by the Group, the outlook for these risks going forward, the implications for the Group should the risk materialise, and the relevant key controls and mitigating factors. These are set out in no order of priority. The Board considers these to be the most significant risks, as such these are risk types which the Board believes could have a material impact on the Group's earnings, capital adequacy and its ability to trade in the future.

These risks should not be regarded as a complete and comprehensive statement of the risks which the Group could be subject to, as there may be risks and uncertainties of which the Group is not aware, or which the Group does not consider significant but which, in the future may become significant. The Group's internal risk identification process goes beyond this assessment and incorporates less material risks and the associated potential Group impact.

The process for identifying and managing risks is set out in more detail within the Risk management report from pages 27 to 28.

Principal Risks	Outlook	Potential Risk Impact	Key Controls and Mitigating Factors
Economic Environment The risk arising from adverse macro-economic conditions in the Group's main market in the UK including Northern Ireland.	**Stable**	Weaker GDP, labour and housing market outcomes would likely result in; • more subdued lending activity with lower demand for mortgage finance, consumer and business credit; • adverse impact in relation to the Group's credit quality of assets; • delayed run-off of back book lending at lower margins. Furthermore any material deterioration in market confidence and resulting disruption in financial and funding markets, as a consequence of a high impact economic or geopolitical event, would likely lead to increased price intensity in retail deposit markets with an adverse impact on deposit margins and therefore the Group's Net Interest Margin.	• Regular reporting framework in place to identify and monitor adverse economic performance against budget including forward looking performance evaluation; • Stress testing performed on a regular basis using macro-economic downside assumptions on which internal Capital and Liquidity Group requirements are based.
Credit Risk The risk of loss resulting from a customer or other counterparty being unable to meet contractual obligations to the Group in respect of loans or other financial transactions	**Decreasing** Consumer credit risk is expected to remain stable. However, a reduction in commercial credit losses is expected based upon the level of provisioning and the improvement in economic conditions.	Should commercial or consumer customers be unable to meet their obligations in relation to borrowing from the Group, the Group may suffer a loss and therefore have an adverse impact on the Group's financial position.	• Credit risk appetite is central to the strategic planning process; • Appropriate segregation of duties in place across the lending end-to-end process including clear separation of business origination and credit underwriting; • Lending authority mandates in place are based on a system of tiered authorities which reflects credit experience and competency; • Each lending and credit unit is subject to regular reviews by a 'third line of defence' Group Credit Review function; • Credit risk appetite based on lending responsibly to manage the credit risk profile of its portfolio within agreed parameters; • Lending and sectoral credit policies which set out, for each type of portfolio, the basis on which credit transactions can be entered into. These policies are reviewed on at least an annual basis; • Impairment policy reviewed on at least an annual basis which sets out the process for the management of deteriorating risk and the recognition of loan losses; • Regular monitoring of lending portfolios by Senior Management and the Credit Risk and Portfolio Committee; • At least annual reviews of all commercial portfolio cases to monitor case specific risk; • Specialist commercial 'Challenged Risk' teams actively managing risk considered to be 'watch-list' grade or below.

1.7 Principal Risks and Uncertainties (continued)

Principal Risks	Outlook	Potential Risk Impact	Key Controls and Mitigating Factors
Regulatory / Legal Risk The risk of failure to meet new or existing regulatory or legislative requirements and deadlines or embed regulatory and legal requirements into processes.	**Increasing** The UK financial services market continues to be subject to a significant period of change in relation to regulation and law e.g. introduction of the mortgage market review. Increasing consumer conduct agenda that increases the level of inherent risk in the retail business.	The Group's operations are subject to both prudential and conduct regulatory oversight exercised by the primary statutory regulatory bodies of financial services within the UK; the PRA and the FCA. The increasing conduct risk agenda necessitates an increase in resources and amendments to current processes which may impact the Group's cost base. The Group could be subject to fines or customer compensation should the Group fail to comply with all aspects of the regulatory regime.	• Business unit regulatory compliance reports are reviewed by and reported to Senior Management as well as the Regulatory and Operational Risk Committee, the Board Risk Committee and the Board; • Regular monitoring of regulatory change (current and proposed) and communication to relevant business owners. • Risk-based regulatory and compliance monitoring performed by an independent compliance monitoring function; • Regular and open communication with the FCA and PRA on all aspects of the Group's activities; • Conduct risk culture and focus embedded into business lines. • Active development of additional conduct measures throughout the UK business including enhanced product approval and review processes.
Operational Risk The risk of loss resulting from inadequate or failed internal controls, processes and systems, or from external events.	**Increasing** Along with other financial service providers, the Group is reliant on IT systems that, with an increase in cyber crime, could be the target of activity by criminals that could lead to disruption of service for customers or financial loss.	The Group could be subject to financial loss or reputational damage as a result of the occurrence of an operational risk. The Group outsources certain services to its Parent and, as a result, the Group's operations are sensitive to operational risk losses arising from outsourcing and technology risk. Furthermore operational risk could result in a loss following failure of internal processes (including financial reporting and risk monitoring processes) or as a result of a fraudulent or criminal act taking place. Litigation proceedings with adverse judgements could result in restrictions or limitations on the Group's operations or result in a material adverse impact on the Group's reputation or financial condition.	• Establishment, implementation and maintenance of a formal approach to the management of operational risk in the form of an 'Operational Risk Management Framework' which defines the Group's approach to identifying, assessing, managing, monitoring and reporting the operational risks that may impact the achievement of the Group's objectives; • Implementation of specific policies and risk mitigation measures for key operational risks, including financial crime (incorporating cyber crime), outsourcing, and business continuity risks; • Arrangements entered into with the Parent are governed through Service Level agreements which are monitored by the Group through formalised governance arrangements, key performance indicators and obligations; • Regular reporting of operational risks to the Regulatory and Operational Risk Committee, Board Risk Committee and the Board.
Liquidity and Funding Risk Risk of a lack of liquid resources to fund the Group's business activities and / or failure to meet payment obligations as they fall due, or being able to do so only at rates substantially above the prevailing market cost of funds.	**Stable**	The Group is primarily funded by way of retail deposits, therefore loss of confidence in the Group's business specifically, or as a result of a systemic shock, could result in unexpectedly high levels of customer deposit withdrawals, which could have a materially adverse effect on the Group's results, financial condition and liquidity prospects. A loss of confidence in the economy generally, the financial services industry or the Group or Parent specifically could lead to a reduction in the Group's ability to access customer deposit funding on appropriate terms in the future and / or to mitigate deposit outflows, both of which would impact on the Group's ability to fund its operations.	• A funding and liquidity risk management framework is in place which is aligned with the Group's overall strategy to be a self-funded business with no sustained funding dependency on the Parent or material dependency on the wholesale funding market; • Daily monitoring and management of the liquidity position including, but not limited to, Early Warning Indicators, metrics, ratios and an escalation process; • Senior Management reporting regularly in relation to liquidity limits and Early Warning Indicators and onward reporting to the Asset and Liability Committee, Board Risk Committee and the Board; • Maintenance of a liquidity pool in excess of 100% of stress outflows from both internal stress scenarios and the regulatory requirements held in either cash or highly marketable liquid assets; • Significant contingent liquidity collateral which is capable of being pledged against borrowings from Central Banks or other external market participants; • Active management of the funding position through specific metrics that determine the amount of on-going new retail deposit acquisition required to fund the Group's asset base.

1.7 Principal Risks and Uncertainties (continued)

Principal Risks	Outlook	Potential Risk Impact	Key Controls and Mitigating Factors
Reputational Risk Risk of loss arising from adverse perception of the Group's image on the part of customers, suppliers, counterparties and regulators.	**Increasing** Expectation of a continued focus on the financial services industry.	Adverse public or industry opinion, resulting from the actual or perceived manner in which the Group conducts its business activities or from actual or perceived practices in the banking industry (such as mis-selling financial products or money laundering), may adversely impact the Group's ability to have a positive relationship with key stakeholders and / or keep and attract customers, and in particular, depositors. Ultimately this may result in an adverse impact to the Group's business, financial condition and prospects.	• The embedding and management of a positive customer conduct culture ensuring that the interests of consumers are at the heart of the Group's operations and management decision-making delivers a positive external view of the Group to customers, regulators and the wider public and community; • Active management of all internal and external communications, focusing on management of political and media relations; • Maintenance of a suite of Early Warning Indicators, the breach of which will trigger escalation and potentially management action such as the invocation of the firms Contingency Plans; • Regular and open dialogue with statutory regulators.
Capital Risk Risk of a lack of capital, which is critical to the Group's ability to operate its businesses and pursue its strategy	**Stable**	Should the Group's capital base be depleted as a result of a materially worse than expected financial performance (including, for example, reductions in earnings as a result of impairment charges or increases in risk weighted assets), the Group would not be able to continue operating.	• Regular Senior Management reporting in relation to forward-looking capital limits and Early Warning Indicators and onward reporting to the Asset and Liability Committee, Board Risk Committee and the Board; • Capital optimisation initiatives linked to an annual Capital Plan reviewed and monitored on a monthly basis; • Comprehensive Individual Capital Adequacy Assessment Process undertaken annually, showing the Group's capital adequacy and capital quality under stress.

Risk Management

Index

	Page
1. Risk Management Framework	**24**
1.1 Risk Governance Structure	24
1.2 Risk Management Organisation	26
1.3 Risk Identity, Strategy and Appetite	27
1.4 Risk Identification, Measurement and Reporting	28
2. Credit Risk	**29**
2.1 Credit Risk	29
2.2 Credit Risk Methodologies	46
3. Financial Risk	**49**
3.1 Liquidity and Funding Risk	49
3.2 Market Risk	54
3.3 Capital Management	56

The information below in sections or paragraphs denoted as audited in sections 2.1, 2.2, 3.1, 3.2 and 3.3 and all the tables (except those denoted unaudited) in the Risk Management Report form an integral part of the audited financial statements as described in the Basis of preparation on page 70.

All other information in the Risk Management Report is additional disclosure and does not form part of the audited financial statements.

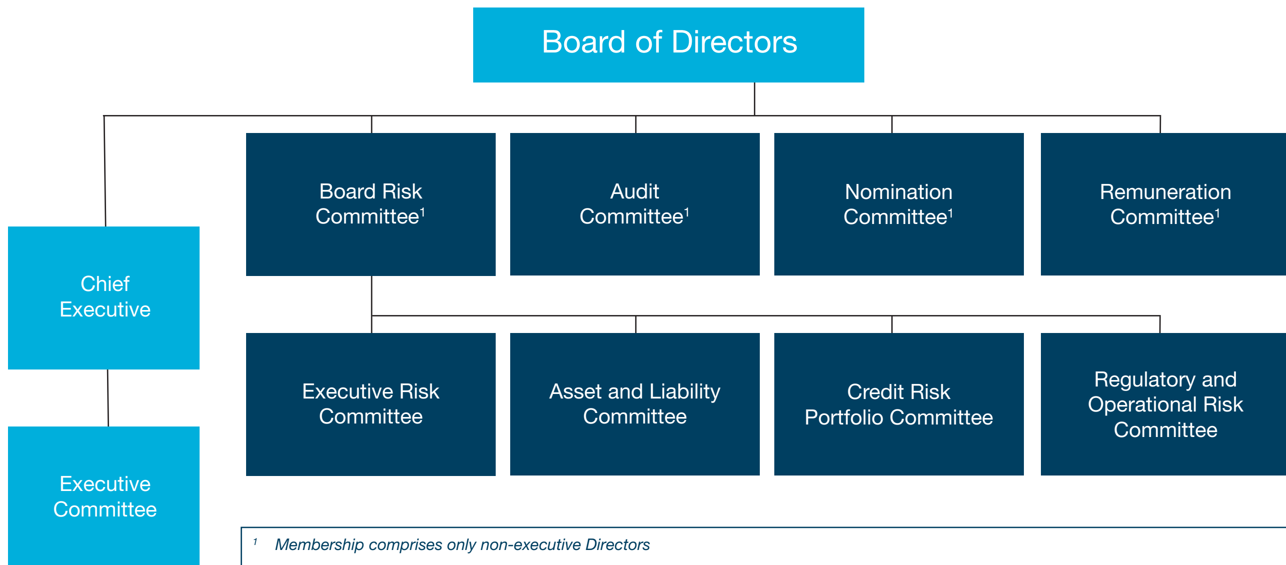
1. Risk Management Framework

The Group has established a Risk Management Framework and Governance structure to effectively ensure that all risks are identified, monitored and managed across its operations including those activities that are outsourced to its Parent and third party suppliers.

The following pages outline the Risk Governance Structure, Risk Management Organisation, Risk Identity, Strategy and Appetite and Risk Monitoring, Management and Reporting. The Group's Principal Risks and Uncertainties are set out on pages 20 to 22 of the Strategic Report.

1.1 Risk Governance Structure

Governance Structure



[1] *Membership comprises only non-executive Directors*

Governance arrangements have remained consistent with the prior year with the Executive Risk Committee, the Asset and Liability Committee (ALCO), the Credit Risk Portfolio Committee (CRPC) and the Regulatory and Operational Risk Committee (RORC) continuing to report to the Board Risk Committee (BRC). While not a formal committee of the Board of Directors (the Board), the Executive Committee supports the Chief Executive Officer (CEO) with his responsibility for the day to day management of the business.

The Board of Directors

The Board is the key governance body and is responsible for the overall strategic direction and the nature and scale of risk that the Group is prepared to assume in order to achieve its corporate objectives. The Board ensures that an appropriate system of internal controls is maintained and reviews its on-going effectiveness.

The Board meets at least seven times a year. It comprises three executives from the Group, four independent non-executive Directors and two non-executive Directors from the Parent company. A number of Board functions are delegated to key Board Committees; including BRC, the Audit Committee, the Remuneration Committee and the Nomination Committee.

Board Risk Committee

BRC's core responsibilities are ensuring that strategy is informed by and aligned with the Group's Risk Appetite and reviewing and reporting to the Board on

1.1 Risk Governance Structure (continued)

the Group's Risk Management Framework. This includes the monitoring of risk governance and ensuring risks are properly identified, assessed, reported and controlled.

BRC meets, at a minimum, four times a year and more frequently as required and its membership is made up of three independent non-executive Directors of the Group. The Chairman of the Board, was also an additional member of the Committee until 31 December 2013.

Audit Committee

The Audit Committee's responsibilities include ensuring the effectiveness of the Group's internal controls incorporating financial controls and risk management systems. Other key responsibilities include monitoring the integrity of the financial statements and ensuring an effective relationship with internal and external auditors is maintained. The Head of Internal Audit for the Group reports to the Chair of the Audit Committee.

The Audit Committee meets, at a minimum, four times a year and more frequently as required and its membership is made up of three independent non-executive Directors of the Group.

Nomination Committee

The Nomination Committee is responsible for reviewing the structure, size and composition of the Board. The Committee is also responsible for succession planning into the Board and the senior management team including FCA Approved Person's appointments. Other responsibilities include agreeing the Corporate Responsibility Policy and overseeing its implementation, monitoring developments in corporate governance and other regulatory developments that are relevant to the assessment of suitability and financial soundness of the holders of key roles within the Group. The Nomination Committee meets, at a minimum, twice a year or more frequently if required and is made up of three non-executive Directors.

The Remuneration Committee

The key responsibility of the Remuneration Committee is to determine and agree with the Board, the broad policy for remuneration and for compliance with the regulations of various regulatory and government bodies including:

- UK Combined Code on Corporate Governance and Schedule A of that Code.
- Relevant laws, regulations, published guidelines and recommendations by the European Banking Authority (EBA) and the Financial Conduct Authority (FCA) / Prudential Regulation Authority (PRA).
- Transaction agreement and the associated letter from the Irish Minister for Finance.

In its deliberations, the Remuneration Committee takes account of relevant market comparisons and practice and where appropriate, is informed by a reasonable assessment of the risk profile, financial situation and future prospects based on input from BRC.

The Remuneration Committee, meets at a minimum, twice a year or more frequently if required, and is made up of three non-executive Directors.

1.2 Risk Management Organisation

The Group's approach to the organisation of risk management is based on the three lines of defence model:

First line of defence has primary responsibility and accountability for risk management and lies with line management in individual businesses or product providers. This applies irrespective of whether or not activities are outsourced to the Parent or to external third parties including strategic partners such as Post Office Limited. Every business unit or product provider is responsible for the identification and management of risk at business unit level, including the implementation of appropriate controls and reporting in respect of all major risk events. Business units are the owners of the risks arising in their businesses and are the first line of defence in managing them.

Second line of defence is the Group's risk management function which is responsible for establishing a risk control framework, formulating risk policy and strategy, providing independent oversight and analysis and centralised reporting of key risks.

Third line of defence is internal audit, which is responsible for providing control assurance to the Board, Audit Committee, senior management and other interested parties, such as regulators and external auditors. This includes the Parent's Group Credit Review (GCR), which is responsible for the review of the quality and management of credit risk assets across the wider organisation, including the Parent. Independence is assured through direct access by internal audit to the Chair of the Group's Audit Committee.

The organisational structure for risk management is designed to facilitate reporting and escalation of risk concerns from business units and risk functions upwards to BRC and to the Board, and the conveying of approved risk management policies and decisions from the Board and BRC to business units.

Where services are provided by the Parent under outsourcing arrangements, the above approach to risk management is embedded in the Master Services Agreement between the Group and the Parent and managed through a series of key service schedules.

In addition, the Group's treasury function is responsible for capital planning and management, liquidity planning and management, transfer pricing, balance sheet management and contingent liquidity programmes. The UK Treasurer reports directly to the Chief Financial Officer (CFO).

1.3 Risk Identity, Strategy and Appetite

Risk Identity
The Group's risk identity sets out that the Group, as a UK retail-focused bank, is committed to long term relationships with its customers and strategic partners.

The customer is at the centre of the Group's business; understanding the customers' needs enables development of successful products, services and channel strategies and allows the Group to ensure that it treats customers fairly. The franchise is focused on generating a return on equity in excess of the cost of capital and a key objective is to achieve balanced growth in customer lending and customer deposits, with a stable funding profile which is appropriate for the asset mix. The Group operates within prudent Board-approved risk parameters.

Risk Strategy
The objectives of the Group's risk strategy are to:

- have clear risk targets and limits, which are aligned to the strategic direction of the Group;
- identify, measure and adequately control all material risks;
- allocate clear roles, responsibilities and accountabilities for the control of risk within the Group; and
- raise awareness of and commitment to the principles of sound risk management throughout the Group.

Risk Appetite
Risk Appetite defines the level of risk that the Group is prepared to accept to achieve its short and medium term strategic objectives. It is defined in qualitative terms, as well as quantitatively, through a series of limits, covering credit risk, market risk, liquidity and funding risk, capital risk and operational risk, including conduct risk. These limits are cascaded into more granular limits and targets across portfolios and business units. Risk appetite guides the Group in its risk taking and related business activities, having regard to the maintenance of financial stability, solvency and the protection of the Group's core franchises and growth platforms. The Group aims to achieve an appropriate balance between risk and returns and to minimise potential adverse effects to its financial performance. The Group has defined measures to track its risk profile against the most significant risks that it assumes.

The Group tracks actual and forecasted results against these limits and these are monitored and reported regularly to Senior Management as well as the appropriate Committee(s).

The Group strives to ensure it operates within its risk appetite and therefore its risk appetite and risk profile must be aligned. Where the Group has a risk profile that is in excess of its risk appetite, it will take action to realign the risk profile through increased risk mitigation activities and risk reduction.

The key risk mitigating activities are set out on page 20 within the Strategic Report.

1.4 Risk Identification, Measurement and Reporting

Risk Identification
Risks facing the Group are identified and assessed through the Group's risk identification process. Risks that are deemed material are included in the Group's Risk Management Framework, owners are identified, appropriate policies are put in place, and a formalised measurement and management process is defined and implemented. The Group regularly reviews the Risk Management Framework and Risk Management policies and systems to reflect changes in markets, products and best market practice. The Group has identified risk types that it believes could have a material impact on earnings, capital adequacy and on its ability to trade in the future and these are covered in the Principal Risks and Uncertainties that are set out on page 20 of the Strategic Report.

Risk Measurement and Reporting
Risk management systems are in place to facilitate measurement, monitoring and analysis of risk. These systems are in line with best practice and ensure compliance with regulatory requirements. In addition to the assessment of individual risks on a case-by-case basis, the Group also measures its exposure to risk at an aggregate level using, among other techniques, risk-adjusted return estimates and stress testing.

The Group conducts stress tests in order to assess the impacts of adverse scenarios on the Group's impairment charges on financial assets, earnings, capital adequacy, liquidity and financial prospects.

The results of stress tests are used to assess the Group's resilience to adverse scenarios and to aid the identification of potential areas of vulnerability. The tests are applied to the existing risk exposure of the Group and also consider changing business volumes, as envisaged in the Group's business plans and strategies. Macroeconomic scenarios of different levels of severity are combined with assumptions on volume changes and margin development.

Stress test results are presented to BRC and the Board as an integral part of the Internal Capital Adequacy Assessment Process (ICAAP) and the Individual Liquidity Adequacy Assessment (ILAA), which assess the risks and capital and liquidity requirements of the Group.

The Group also performs reverse stress testing, primarily a qualitative process to derive severe stress scenarios which would breach the Group's ability to survive unassisted, thus helping to define risk tolerance boundaries for the business.

Risk Reporting
Risks are measured, reported and monitored by the Group on a daily, weekly, monthly and / or quarterly basis depending on the materiality of the risk.
On a quarterly basis, material risks identified under the Group's Risk Management Framework are assessed and their status is reported in the Quarterly Risk Report in the first instance. This report is submitted to BRC and the Board.

The format of this report is approved by BRC. The content of the quarterly report includes analysis of, and commentary on, all material risk types. It also addresses governance and control issues and the Group's capital position. In addition to the quarterly report, BRC and the Board consider more frequent formal updates on the key areas of credit and liquidity risk and capital management.

The reports also provide data on the external economic environment and management's view of the implications of this environment on the Group's risk profile. BRC also receives risk information through the review of minutes from the Executive Risk and other committees.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:31 Page 29

2.1 Credit Risk

Key points:

- Gross loans and advances to customers remain predominantly in line with 2012 at £18.6 billion.
- The credit environment in which the Group operated remained challenging, but improved from 2012.
- The commercial property sector continues to be characterised by low levels of activity, illiquid markets and continued pressure in the Northern Ireland land and development portfolio, as well as in retail sectors where downward pressure on rents, some high profile administrations, weaker consumer spending and sentiment are negatively impacting trading conditions.
- Total customer impairment charges have reduced from £183 million at 31 December 2012 to £125 million at 31 December 2013 due to lower commercial impairment charges.
- The residential mortgage portfolio has continued to perform well. Arrears and default rate performance continues to be ahead of expectations.
- The consumer lending portfolios performed ahead of expectations, despite the weakness in general consumer confidence impacting on new business volumes.

Definition (audited)

Credit risk is the risk of loss resulting from a counterparty being unable to meet its contractual obligations to the Group in respect of loans or other financial transactions. Credit risk includes default risk, recovery risk, counterparty risk, cross border (or transfer) risk, country risk, credit concentration risk and settlement risk. The nature of the Group's exposure to credit risk, the manner in which it arises, policies and processes for managing credit risk, and the methods used to measure and monitor credit risk are set out below.

How Credit Risk Arises

Credit risk arises from loans and advances to customers. It also arises, in the form of counterparty credit risk, from the financial transactions the Group enters into with financial institutions, sovereigns and state institutions. The main types of financial transactions the Group enters into, and which give rise to credit risk, are loans and advances to customers and its investments in liquid assets. Credit risk on loans and advances to customers arises as a result of the amounts it has actually lent and the amounts which it has committed to lend. Such commitments take a number of forms and are discussed further below.

With regard to commitments, the Group could potentially suffer loss to an amount equivalent to its total unused commitments. However, the Group does not expect to incur losses to that extent, as most consumer related commitments can be cancelled, and non-consumer commitments are extended subject to the customer continuing to achieve specific credit standards. The Group is also exposed to credit risk through its derivatives, available for sale assets, and other financial assets.

Credit Policy

The core values and principles governing the provision of credit are contained in the Statement of Credit Policy, which is approved by BRC. Individual sector/portfolio-level credit policies define in greater detail the credit approach appropriate to those sectors or portfolios. These policies take account of the Group's Risk Appetite Statement, applicable sectoral credit limits, the markets in which the Group operates and the products provided. Each staff member involved in developing customer relationships and / or assessing or managing credit, has a responsibility to ensure compliance with these policies. Procedures for the approval and monitoring of exceptions to policy are included within the policy documents.

Credit Risk Management - Retail and Commercial Lending (audited)

The management of credit risk is focused on a detailed analysis at origination, followed by early intervention and active management of accounts where creditworthiness has deteriorated. The Chief Credit Officer (CCO) – Commercial has responsibility for credit management of the Business Banking book and oversight of the NIIB book, while the Chief Credit Officer (CCO) – Retail has similar responsibility for the Retail Lending book. Supported by the broader Risk function, the CCOs are responsible for overall risk reporting to the Executive Committee, BRC and the Board. These functions report to the Chief Risk Officer (CRO), who reports directly to the CEO. The Risk function, under the management of the CRO, provides independent oversight and management of the Group's credit risk strategy and credit risk management information, as well as the Group's suite of credit risk policies.

Lending Authorisation (audited)

The Group's credit risk management systems operate through a hierarchy of lending authorities, which are linked to internal customer loan ratings and limits. All exposures which exceed prescribed levels require approval or ratification by BRC.

Other exposures are approved by personnel according to a system of tiered individual authorities, which reflect credit competence, proven judgement and experience. Material lending proposals are referred to credit underwriting units for independent assessment and approval, or formulation of a recommendation and subsequent adjudication by the appropriate approval authority.

2.1 Credit Risk (continued)

Credit Related Commitments (audited)
The Group classifies and manages credit related commitments that are not reflected as loans and advances on the balance sheet, as follows:

Guarantees and irrevocable standby letters of credit: irrevocable commitments by the Group to make payments at a future date, in specified circumstances, on behalf of a customer. These instruments are assessed on the same basis as loans for credit approval and management.

Commitments: unused elements of authorised credit in the form of loans, guarantees or letters of credit, where the Group is potentially exposed to loss in an amount equal to the total unused commitments. The likely amount of loss is less than the total unused commitments, as most commitments are contingent upon customers maintaining specific credit and performance standards. These instruments are assessed on the same basis as loans for credit approval and management.

Letters of offer: where the Group has made an irrevocable offer to extend credit to a customer and the customer may, or may not, have confirmed acceptance of the offer on the terms outlined and within the specified timeframe. The exposure is assessed on the same basis as loans for credit approval and management. The ultimate exposure to credit risk is considerably less than the face value of offer letters, as not all offers are accepted.

Credit Reporting / Monitoring (audited)
It is Group policy to ensure that adequate up-to-date credit management information is available to support the credit management of individual account relationships and the overall loan portfolio. Information is produced on a timely basis and at a frequency interval that reflects the purpose of the report. Credit risk information at a product / sector level is reported on a monthly basis to senior management. This monthly reporting includes detailed information on loan book volume, the quality of the loan book (credit grade and probability of default (PD) profiles), concentrations and loan impairment provisions, including details of any large individual impaired exposures. Performance against specified credit risk limits, as detailed in the risk appetite statement, is monitored and reported to senior management and to BRC. The format of reports and commentaries are consistent across the Group to enable an assessment of trends in the loan book. Along with the regular suite of monthly and quarterly reporting, ad hoc reports are submitted to senior management / BRC as required. GCR, an independent function within the Parent (part of the Parent's Internal Audit function) and an outsourced service provider to the Group, reviews the quality and management of credit risk assets across the Group and reports to BRC on a quarterly basis. The reviews detail levels of adherence to credit policies and credit procedures across the various portfolios on behalf of the Group. GCR also considers the timeliness of the individual credit file review process and the quality of credit assessment in each portfolio.

Monthly portfolio review meetings covering the NI and GB challenged portfolios are also conducted. These are attended from the business by the heads of business banking and the heads of the challenged units, by the CRO, the CCO - Commercial and the head of challenged credit.

Group risk personnel and finance senior management review and confirm the appropriateness of impairment provisioning methodologies and the adequacy of impairment provisions on a half yearly basis. Their conclusions are reviewed by the Parent's Credit and Market Risk function, the Parent's Group Risk Policy Committee (GRPC) and BRC. Impairment provisioning methodologies are approved on a half yearly basis by GRPC. As part of the review process, consideration is given as to whether there is a need to apply an additional management overlay to take account of portfolio effects, for example significant deterioration in the economy, negative market price movements etc.

Credit Risk Management - Additional Commercial Lending Practices (audited)
In relation to the commercial credit management processes, specialist challenged risk units manage commercial loans below a certain grade quality threshold. To ensure timely intervention in deteriorating risk this includes both 'unsatisfactory' (grade 10-12) and watch-list cases which are at the lower end of acceptable (grade 9). Refer to page 34 for further details on credit grades.

Credit Risk Mitigation
An assessment of the borrower's ability to service and repay the proposed level of debt is undertaken for credit requests and is the primary component of the Group's approach to mitigating risk.

In addition, the Group mitigates credit risk through both the adoption of preventative measures (e.g. controls and limits) and the development and implementation of strategies to assess and reduce the impact of particular risks, should these materialise (e.g. securitisation and collateralisation).

Collateral
Credit risk mitigation includes the requirement to obtain collateral, depending on the nature of the product and local market practice, as set out in the Group's policies and procedures. The nature and level of security required depends on a number of factors, including, but not limited to, the amount of the exposure, the type of facility provided, the term of the facility, the amount of the borrower's own cash input and an evaluation of the level of risk or probability of default. The Group takes collateral as a secondary source of repayment which can be called upon if the borrower is unable or unwilling to service and repay debt as originally assessed.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:31 Page 31

2.1 Credit Risk (continued)

A variety of types of collateral are accepted, as follows:

- residential and commercial real estate;
- physical collateral (motor vehicles, plant and machinery, stock etc.);
- financial collateral (lien over deposits, shares etc.); and
- other collateral (debtors, guarantees, insurance etc.).

The Group's requirements around completion, valuation and management of collateral are set out in appropriate Group or business unit policies and procedures. The extent to which collateral mitigates credit risk in respect of the Group's mortgage portfolio, is set out on page 38.

Methodologies for valuation of collateral

Details of the valuation methodologies are set out in the Credit Provisioning Methodologies section on page 48.

Mortgage Indemnity Guarantee - Mortgage Portfolios

Mortgage indemnity guarantee is an insurance policy which can compensate a lender for a loss following the sale of the property by the lender as mortgagee in possession. The Group purchases such cover for all loans at the point of origination where the Loan to Value exceeds 75%. The policy utilised by the Group is provided through a captive insurance company which is a wholly owned subsidiary of the Parent.

Forbearance Strategies

Forbearance occurs when a borrower is granted a temporary or permanent concession or agreed change to a loan ('forbearance measure') for reasons relating to the actual or apparent financial stress or distress of that borrower. If the concession or agreed change to a loan granted to a borrower is not related to the actual or apparent financial stress or distress of that borrower, forbearance has not occurred. A loan which has an active 'forbearance measure' is a 'forborne loan'.

A range of forbearance strategies are used by the Group for customers in arrears or facing potential arrears on contracted loan repayments, in order to arrange, where viable, sustainable short term or longer term repayment solutions as appropriate. A forbearance strategy may include, but is not necessarily limited to, one or more of the following measures:

- term extension: an arrangement where the original term of the loan is extended.
- adjustment or non-enforcement of covenants: an arrangement whereby the Group agrees to either waive an actual or expected covenant breach for an agreed period, or adjust the covenant(s) to reflect the changed circumstances of the borrower;
- reduced payments (interest only): an arrangement where the borrower pays interest only on the principal balance, on a temporary or longer term basis, with the principal balance unchanged, rather than repaying some of the principal as required under the original facility agreement;
- facilities in breach of terms placed on demand: an arrangement whereby the Group places a facility in breach of its contractual terms on a demand basis as permitted under the facility agreement rather than enforcing, and pending a more long term resolution;
- reduced payment (greater than interest only) incorporating some principal repayments: a temporary or medium term arrangement where the borrower pays the full interest due plus an element of principal due on the basis that principal payments will increase in the future; and
- capitalisation of arrears: an arrangement whereby arrears are added to the principal balance, effectively clearing the arrears, with either the repayments or the original term of the loan adjusted accordingly to accommodate the increased principal balance.

Impaired loans that have received forbearance are recorded and reported in the 'Impaired' category. Any other loan that has received forbearance is recorded and reported within the appropriate 'past due but not impaired' or 'neither past due nor impaired' rating category as described on page 34.

For business banking the monitoring of forbearance measures follows the normal review cycle for individual customer exposures based on amount and credit grade, as set out in the Credit Policy.

Mortgage accounts that are subject to forbearance are monitored and reviewed by way of monthly management information reporting. This includes tracking the aggregate level of default arrears that emerge on the forborne elements of the loan book.

The impairment provisioning approach and methodologies are set out in each of the portfolio-level Impairment Policies. An 'incurred loss' model is followed for all exposures, whether or not forbearance has been granted.

Loan Loss Provisioning

Through its on-going credit review processes, the Group seeks early identification of deteriorating loans, with a view to taking corrective action to prevent the loan becoming impaired. Typically, loans that are at risk of impairment are managed by dedicated specialist units / debt collection teams focused on working out loans.

The identification of loans for assessment as impaired is driven by the Group's credit risk rating systems and by trigger events identified in the Group's credit and impairment policies. It is the Group's policy to provide for impairment promptly and consistently across the loan book. For those loans that become impaired, the focus is to minimise the loss that the Group will incur from such impairment. This may involve entering into restructuring arrangements, or taking action to enforce security.

2.1 Credit Risk (continued)

Other factors taken into consideration in estimating provisions include the economic climate, changes in portfolio risk profile and the effect of any external factors, such as legal or regulatory requirements.

Under delegated authority from the Board, the Group's Impairment policy is approved annually by BRC.

The Group's provisioning methodology is approved by the CRPC on a half yearly basis, details of which are set out in Credit Risk Methodologies section on pages 46 to 48. The quantum of the Group's impairment charge, impaired loan balances, and provisions are also reviewed by BRC annually, in advance of providing a recommendation to the Audit Committee.

An analysis of the Group's impairment provisions at 31 December 2013 is set out on pages 35 to 37 and note 17.

Counterparty Credit Risk

The continued weak international financial environment means that the Group continues to be exposed to increased counterparty risk. The Group has implemented a number of measures to mitigate this increased risk. These include:

- reduced individual Group exposures across a wider spread of banking institutions;
- strict credit risk management procedures; and
- application of tighter credit policy criteria, where required.

The Group's net exposure to the Parent (disclosed gross within loans and advances to banks, deposits from banks, derivative assets and derivative liabilities) is in relation to the Group's market risk management. The gross risk is managed through a contractual master netting agreement with the Parent whereby, in the event of a default by either party, all amounts due or payable will be settled immediately on a net basis. Furthermore, derivatives executed with the Parent are subject to an ISDA and CSA and therefore collateral requirements are calculated daily and posted as required. The net exposure to the Parent is measured and monitored on a daily basis and is maintained within the Group's large exposure limits.

BRC is responsible for establishing an appropriate policy framework for the prudential management of treasury credit risk, including net exposure to the Parent. Credit counterparties are subject to on-going credit review and exposures are monitored on a daily basis.

Large Exposures

The Group's risk appetite statement, credit policy and regulatory guidelines set out the maximum exposure limits to a customer, or a group of connected customers. The policy and regulatory guidelines cover both exposures to the Parent and other counterparties. Regulatory guidelines limit risk concentration in individual exposures. No single exposure exceeded regulatory guidelines during the year, including net exposures to the Parent.

Loans and advances to banks at 31 December 2013 of £12,824 million include £11,646 million due from the Parent, whilst deposits from banks at 31 December 2013 of £11,660 million include £11,651 million due to the Parent. At 31 December 2013, the Group therefore has a net exposure under these two categories due to the Parent of £5 million (31 December 2012: £148 million net exposure from the Parent).

At 31 December 2013 derivative assets and derivative liabilities include £4 million and £7 million respectively with the Parent and therefore a net exposure due to the Parent of £3 million (31 December 2012: £3 million and £6 million respectively and therefore a net exposure due to the Parent of £3 million).

Credit Concentration Risk

Credit concentration risk is the risk of loss due to exposure to a single entity, or group of entities, engaged in similar activities and having similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. Undue concentrations could lead to increased or unexpected volatility in the Group's earnings. Management of risk concentrations is an integral part of the Group's approach to risk management. The Group imposes risk control limits and guide points to mitigate significant concentration risk. These limits are formed by the Group's risk appetite, and that of the Parent, and are set in the context of the Group's risk strategy. Monetary limits are set by CRPC and, where necessary, approved by BRC. Single name concentrations are also subject to limits.

The Group's primary market is the UK and loans, originated and managed in the UK, represent a material concentration of credit risk.

The Group's residential mortgage portfolio is widely diversified by individual borrower and amounted to 70% of total loans as at 31 December 2013 (67%; 31 December 2012). By product type, the residential mortgage portfolio is made up of standard owner occupier (55%), self-certified owner occupier (9%) and Buy to Let (BTL) (36%) (31 December 2012: 58%, 10%, and 32% respectively). In terms of geographical concentrations, the largest concentration is the London and South East area at 49% (31 December 2012: 46%). The Group's concentration of residential mortgages in Northern Ireland is 4% of the portfolio (31 December 2012: 4%). Product type and geographic concentrations are monitored and reported in accordance with the monetary limits set by BRC.

The property and construction sector, which includes investment property and landbank, accounted for 13%, or £2.4 billion, of total loans at 31 December 2013 (31 December 2012: 16% or £3.1 billion).

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:31 Page 33

2.1 Credit Risk (continued)

Book Profile – Loans and Advances to Customers

The following table gives a breakdown by industry of the Group's gross loans and advances to customers.

Total loans - by industry analysis (audited)	**31 December 2013 £m**	31 December 2012 £m
Residential mortgages	13,078	12,568
Finance leases and hire purchase	803	717
Credit cards	372	399
Property and construction	2,455	3,074
Business and other services	1,290	1,248
Manufacturing and distribution	360	394
Other	289	313
Total	**18,647**	**18,713**

Asset Quality – Loans and Advances to Customers

31 December 2013 **Risk profile of loans and advances to customers (before impairment provisions) (audited)**	**Residential mortgages £m**	**Non-property SME and corporate £m**	**Property and construction £m**	**Consumer £m**	**Total loans and advances to customers £m**	**Total loans and advances to customers %**
High quality	12,427	622	78	1,040	14,167	76%
Satisfactory quality	21	835	605	-	1,461	8%
Acceptable quality	49	129	282	-	460	2%
Lower quality but not past due nor impaired	-	118	320	-	438	2%
Neither past due nor impaired	**12,497**	**1,704**	**1,285**	**1,040**	**16,526**	**88%**
Past due but not impaired	504	18	109	24	655	4%
Impaired	77	294	1,061	34	1,466	8%
Total	**13,078**	**2,016**	**2,455**	**1,098**	**18,647**	**100%**

31 December 2012 Risk profile of loans and advances to customers (before impairment provisions) (audited)	Residential mortgages £m	Non-property SME and corporate £m	Property and construction £m	Consumer £m	Total loans and advances to customers £m	Total loans and advances to customers %
High quality	11,981	531	90	1,026	13,628	73%
Satisfactory quality	146	870	966	-	1,982	11%
Acceptable quality	-	158	451	-	609	3%
Lower quality but not past due nor impaired	-	140	267	-	407	2%
Neither past due nor impaired	12,127	1,699	1,774	1,026	16,626	89%
Past due but not impaired	375	31	113	29	548	3%
Impaired	66	250	1,187	36	1,539	8%
Total	12,568	1,980	3,074	1,091	18,713	100%

2.1 Credit Risk (continued)

Asset Quality - Financial Assets
In line with the requirements of IFRS 7 the Group classifies financial assets as:

- neither past due nor impaired;
- past due but not impaired; and
- impaired;

The Group uses internal ratings, based on an assessment of the credit quality of the customer, as part of its credit risk management system. A thirteen point credit grade rating scale is used for more complex, individually managed exposures, including commercial and business lending. A seven-point credit grade rating scale is used for standard products (including mortgages, personal and small business loans). Both credit scales have a defined relationship with the Group's Probability of Default (PD) scale.

Other financial assets are assigned an internal rating, supported by external ratings of the major rating agencies.

'Neither past due nor impaired' ratings are defined as follows:

- high quality ratings apply to highly rated financial obligors, strong corporate and business counterparties and consumer banking borrowers (including residential mortgages), with whom the Group has an excellent repayment experience. High quality ratings are derived from grades 1 to 4 on the thirteen-point grade scale, grades 1 and 2 on the seven-point grade scale, and ratings equivalent to AAA, AA+, AA, AA-, A+, A, A-, BBB+ and BBB for the external major rating agencies;
- satisfactory quality ratings apply to good quality financial assets that are performing as expected, including loans and advances to small and medium sized enterprises, leveraged entities and more recently established businesses. Satisfactory quality ratings also include some element of the Group's retail portfolios. Satisfactory quality ratings are derived from grades 5 to 7 on the thirteen point grade scale, grade 3 on the seven-point grade scale, and external ratings equivalent to BBB-, BB+, BB and BB-;
- acceptable quality ratings apply to customers with increased risk profiles, that are subject to closer monitoring and scrutiny by lenders, with the objective of managing risk and moving accounts to an improved rating category. Acceptable quality ratings are derived from grades 8 and 9 on the thirteen-point grade scale, grade 4 on the seven-point scale and external ratings equivalent to B+; and
- the lower quality but not 'past due but not impaired' rating applies to those financial assets that are neither in arrears nor impaired, but where the Group requires a work down or work out of the relationship, unless an early reduction in risk is achievable. Lower quality ratings are derived from outstanding balances within rating grades 10 and 11 on the thirteen-point grade scale, grade 5 on the seven point grade scale, and external ratings equivalent to B or below.

'Past due but not impaired loans' are defined as follows:

- loans excluding residential mortgages, where repayment of interest and / or principal are overdue by at least one day, but are not impaired; and
- residential mortgages may be 'past due but not impaired', in cases where the loan to value (LTV) ratio on the mortgage indicates no loss in the case of default by the borrower to the Group.

'Impaired loans' are defined as follows:

- loans with a specific impairment provision attaching to them;
- loans (excluding residential mortgages) which are more than 90 days in arrears;
- all assets in grades 12 and 13 on the thirteen-point grade scale and grades 6 and 7 on the seven-point grade scale are impaired; and
- residential mortgages are only classified as impaired when there is a specific provision against them.

Refer to page 46 for details on the loan loss provisioning methodology.

2.1 Credit Risk (continued)

Financial Assets - 'past due but not impaired': Loans and advances to customers

The table below provides an aged analysis of financial assets 'past due but not impaired', by asset classification. Amounts arising from operational / timing issues, that are outside the control of customers, are generally excluded.

31 December 2013 (audited)	Residential mortgages £m	Non-Property SME and corporate £m	Property and construction £m	Consumer £m	Total £m
Past due up to 30 days	101	10	29	11	151
Past due 31-60 days	240	6	44	9	299
Past due 61-90 days	64	2	36	4	106
Past due more than 90 days	99	-	-	-	99
Total	**504**	**18**	**109**	**24**	**655**

31 December 2012 (audited)	Residential mortgages £m	Non-Property SME and corporate £m	Property and construction £m	Consumer £m	Total £m
Past due up to 30 days	67	14	10	15	106
Past due 31-60 days	173	10	77	10	270
Past due 61-90 days	56	7	26	4	93
Past due more than 90 days	79	-	-	-	79
Total	375	31	113	29	548

There was an increase in the total Past Due, but not impaired balances from £548 million to £655 million primarily due to movements in residential mortgages. Arrears on residential mortgage balances increased £129 million, primarily within the owner occupier segment. This increase on residential mortgages was offset by improved positions in the consumer and commercial segments of the loan book.

Financial Assets - 'Impaired': Loans and advances to customers

31 December 2013 (audited)	Advances £m	Impaired loans £m	Impaired loans as % of advances £m	Impairment provisions £m	Impairment provisions as % of impaired loans £m
Residential mortgages	13,078	77	1%	41	53%
Non-property SME and corporate	2,016	294	15%	131	45%
Property and construction	2,455	1,061	43%	513	48%
Consumer	1,098	34	3%	34	100%
Total	**18,647**	**1,466**	**8%**	**719**	**49%**

2.1 Credit Risk (continued)

31 December 2012 (audited)	Advances £m	Impaired loans £m	Impaired loans as % of advances £m	Impairment provisions £m	Impairment provisions as % of impaired loans £m
Residential mortgages	12,568	66	1%	44	67%
Non-property SME and corporate	1,980	250	13%	104	42%
Property and construction	3,074	1,187	39%	511	43%
Consumer	1,091	36	3%	36	100%
Total	18,713	1,539	8%	695	45%

Loans and advances to customers classified as 'impaired' amounted to £1.5 billion, or 8%, of the Group's loan book at 31 December 2013 (31 December 2012: £1.5 billion, or 8%).

Property and construction loans classified as 'impaired' are £1.1 billion at 31 December 2013 (31 December 2012: £1.2 billion), reflecting the difficulties facing residential developments, particularly in Northern Ireland, as well as continued weak conditions in the investment property element of this loan portfolio.

The volume of non-property SME and corporate loans that are classified as 'impaired' has increased, from £250 million at 31 December 2012, to £294 million at 31 December 2013. This increase reflects the impact of subdued economic conditions in the UK.

Consumer loans that are 'impaired' are £34 million at 31 December 2013 (31 December 2012: £36 million), reflecting improved arrears performance in the consumer books.

Impairment provision by nature of impairment provision (audited)	**31 December 2013 £m**	31 December 2012 £m
Specific provisions	635	613
Incurred but not reported (IBNR)	84	82
Total impairment provision	**719**	**695**

Specific provisions increased by 4% to £635 million at 31 December 2013, from £613 million at 31 December 2012, partly due to a continued deterioration in the commercial portfolio. Incurred but not reported provisions increased from £82 million at the end of December 2012 to £84 million at the end of December 2013, an increase of 2% for the year, mainly in relation to the retail portfolio.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:32 Page 37

2.1 Credit Risk (continued)

Impairment charge (audited)	Year ended 31 December 2013 Specific £m	IBNR £m	Total £m	Year ended 31 December 2012 Specific £m	IBNR £m	Total £m
Residential mortgages	5	3	8	9	5	14
Non-property SME and corporate	34	-	34	27	2	29
Property and construction	69	-	69	132	(10)	122
Consumer	14	-	14	17	1	18
Total loan impairment charge / (release)	**122**	**3**	**125**	**185**	**(2)**	**183**

Whilst UK economic conditions improved during 2013, and loan losses have fallen significantly, the recent UK recession continued to impact with elevated unemployment levels, low earnings growth, and weak consumer sentiment and business confidence. Whilst conditions improved in some property sectors/regions continuing low transaction levels and weak demand in certain markets continued to impact on impairment charges, particularly in the commercial property portfolios.

Impairment charges on loans and advances to customers decreased by £58 million from £183 million for the year ended 31 December 2012 to £125 million for the year ended 31 December 2013.

The impairment charge on residential mortgages decreased by £6 million, from £14 million for the year ended 31 December 2012, to £8 million for the year ended 31 December 2013. This was primarily due to the increase in property values experienced during the year. The volume of mortgages past due, however, increased with some customers coming under pressure from fixed income at a time of increasing prices.

The impairment charge on the non-property SME and corporate loan portfolio was £34 million for the year ended 31 December 2013, compared to £29 million for the year ended 31 December 2012. Rising inflation, combined with concerns regarding the impact of fiscal austerity, have left UK economic conditions subdued and resulted in an increased impairment charge.

The impairment charge of £69 million on the property and construction portfolio, for the year ended 31 December 2013, has decreased from £122 million for the year ended 31 December 2012 as a result of an improvement in economic conditions.

The impairment charge of £14 million on consumer loans, for the year ended 31 December 2013 has decreased by £4 million, from £18 million for the year ended 31 December 2012. Default arrears on this portfolio were below expectations, with consumer demand for credit subdued, impacting on loan book growth and consequently on the quantum of incurred but not reported provisions in respect of this portfolio.

2.1 Credit Risk (continued)

The following tables set out an analysis of the loan to value profile of the Group's mortgage book as at 31 December 2013 and 31 December 2012.

31 December 2013 Loan to value (LTV) ratio of total mortgages (audited)	**Standard**	**Buy to let**	**Self certified**	**Total mortgage portfolio**
	% of book	**% of book**	**% of book**	**% of book**
Less than 50%	20%	13%	15%	17%
51% to 70%	24%	38%	30%	30%
71% to 80%	24%	26%	21%	24%
81% to 90%	20%	15%	19%	18%
91% to 100%	8%	6%	12%	8%
Subtotal	**96%**	**98%**	**97%**	**97%**
101% to 120%	4%	2%	3%	3%
Greater than 120%	-	-	-	-
Total	**100%**	**100%**	**100%**	**100%**
Weighted average LTV[1]:				
Stock of mortgages at year end[1]	**73%**	**75%**	**75%**	**74%**
New mortgages during year[1]	**77%**	**71%**	**n/a**	**76%**

31 December 2012 Loan to value (LTV) ratio of total mortgages (audited)	Standard	Buy to let	Self certified	Total mortgage portfolio
	% of book	% of book	% of book	% of book
Less than 50%	19%	9%	12%	15%
51% to 70%	15%	24%	22%	19%
71% to 80%	18%	27%	19%	21%
81% to 90%	24%	23%	20%	23%
91% to 100%	16%	11%	19%	14%
Subtotal	92%	94%	92%	92%
101% to 120%	7%	6%	8%	7%
Greater than 120%	1%	-	-	1%
Total	100%	100%	100%	100%
Weighted average LTV[1]:				
Stock of mortgages at year end[1]	73%	75%	75%	74%
New mortgages during year[1]	77%	71%	n/a	76%

[1] *Weighted Average LTVs are calculated at a property level and reflect the average of property values in proportion to the outstanding mortgage.*

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:32 Page 39

2.1 Credit Risk (continued)

Forbearance Arrangements for Residential Mortgages (unaudited)

31 December 2013 Forbearance arrangements (before impairment provisions)	**Loans not in default[1]**		**Loans > 90 days past due and / or impaired**		**All loans**	
	Balance £m	**Number of accounts[2]**	**Balance £m**	**Number of accounts[2]**	**Balance £m**	**Number of accounts[2]**
Total						
Term extension	13	191	1	9	14	200
Interest only	61	537	7	48	68	585
Capitalisation of arrears	14	78	2	9	16	87
Other	2	15	-	2	2	17
Total	**90**	**821**	**10**	**68**	**100**	**889**

31 December 2012 Forbearance arrangements (before impairment provisions)	Loans not in default[1]		Loans > 90 days past due and / or impaired		All loans	
	Balance £m	Number of accounts[2]	Balance £m	Number of accounts[2]	Balance £m	Number of accounts[2]
Total						
Term extension	11	162	-	7	11	169
Interest only	70	602	10	72	80	674
Capitalisation of arrears	14	72	2	10	16	82
Other	1	13	-	2	1	15
Total	**96**	**849**	**12**	**91**	**108**	**940**

[1] *Loans neither > 90 days past due nor impaired.*
[2] *The number of accounts does not equate to either the number of customers or the number of properties.*

The Group has an operating infrastructure in place to assess and to implement restructure arrangements for customers on a case-by case basis. Arrears are not generally capitalised at the point of restructure and remain in the applicable past due category. Details of the Group's forbearance strategies are set out on page 31.

2.1 Credit Risk (continued)

Forbearance Arrangements for Commercial loans (unaudited)

31 December 2013 Forbearance arrangements (before impairment provisions)	Property and construction Land and development £m	Investment £m	Total £m	Non-property SME and corporate £m	Total forborne loans and advances customers £m
Term extension	47	464	511	66	577
Adjustment or non-enforcement of covenants	-	49	49	23	72
Interest only	2	11	13	30	43
Facilities in breach of terms placed on demand	6	34	40	5	45
Reduced payment (greater than interest only)	1	27	28	5	33
Capitalisation of arrears	-	1	1	-	1
Other	1	17	18	32	50
Total forborne loans and advances to customers	**57**	**603**	**660**	**161**	**821**

31 December 2012 Forbearance arrangements (before impairment provisions)	Property and construction Land and development £m	Investment £m	Total £m	Non-property SME and corporate £m	Total forborne loans and advances customers £m
Term extension	47	301	348	77	425
Adjustment or non-enforcement of covenants	-	63	63	43	106
Interest only	6	7	13	44	57
Facilities in breach of terms placed on demand	21	225	246	17	263
Reduced payment (greater than interest only)	3	30	33	22	55
Capitalisation of arrears	-	1	1	2	3
Other	1	11	12	21	33
Total forborne loans and advances to customers	**78**	**638**	**716**	**226**	**942**

The above table illustrates commercial loans that have been subject to restructuring arrangements. These arrangements may be temporary or permanent and are subject to individual case assessment, taking into account the circumstances and risk profile of the customer.

Property and Construction

(a) Investment

This category represents 73% of the total forborne commercial loans as at 31 December 2013, which reflects weak conditions in both the residential and commercial property markets. The need for forbearance was principally caused by falling property values rather than reduced rental income. 'Term extensions' account for 77% of all forbearance measures and a further 6% were 'placed on demand', mainly because opportunities to refinance property debt with other banks are limited.

However, in such cases scheduled loan payments continue to be met. Covenant adjustments or waivers were considered sufficient on a further 8% of forborne loans, partly reflecting the impact on 'maximum LTV' covenants of reduced property values. Property loan repayments are not normally reduced unless the rental income generated by the property decreases; consequently, a full or partial waiver of capital repayments accounted for only 6% of forbearance measures.

(b) Land and Development (L&D)

Due to the high incidence of impaired loans, this category accounts for only 7% of total forborne commercial loans. 'Term extensions' of 82% and 'placed on demand' of 11% were the most common forbearance measures applied to L&D loans, followed by a full or partial waiver of capital repayments of 5%.

Non-Property SME and Corporate

Forbearance measures have been granted to 9% of non-impaired exposures in this category (compared to 46% for Investment Property and 80% for L&D). This is consistent with the generally stronger credit quality of SME / Corporate sector exposures compared to those in

2.1 Credit Risk (continued)

the Property and Construction sector. It also partly reflects the greater number of options typically available to the SME / Corporate sector to deal with adverse trading conditions – for example by reducing overheads, finding new markets, renegotiating terms with suppliers, etc. – before the ability to continue meeting debt servicing commitments is jeopardised. The foregoing is reflected in the type of forbearance measures provided to SME / Corporate borrowers, with 41% granted 'term extensions', 22% permitted a full or partial waiver of capital repayments, and 3% 'placed on demand'.

Repossessed Collateral on Mortgages

During the year ended 31 December 2013, the Group took possession of collateral held as security on mortgages, as follows:

	31 December 2013		31 December 2012	
Repossessed collateral (audited)	**Number of repossessions as at balance sheet date Number**	**Balance outstanding £m**	Number of repossessions as at balance sheet date Number	Balance outstanding £m
Residential repossessions				
Owner occupier	21	3	23	3
Buy to let	21	3	53	6
Self certified	10	2	15	3
Total	**52**	**8**	**91**	**12**

2013 Repossessed collateral (unaudited)	**Number of disposals during the year Number**	**Balance outstanding at repossession £m**	**Net Sales proceeds received £m**
Residential repossessions			
Owner occupier	74	5	6
Buy to let	107	7	8
Self certified	34	6	6
Total residential repossessions	**215**	**18**	**20**

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:32 Page 42

2.1 Credit Risk (continued)

Repossessed Collateral on loans

During the year ended 31 December 2013, the Group took possession of collateral held as follows:

Repossessed collateral (audited)	**31 December 2013** Number of repossessions as at balance sheet date Number	**31 December 2013** Balance outstanding £m	31 December 2012 Number of repossessions as at balance sheet date Number	31 December 2012 Balance outstanding £m
Property and construction	59	5	40	21
Total	**59**	**5**	**40**	**21**

2013 Repossessed collateral (unaudited)	Number of disposals during the year Number	Balance outstanding at repossession £m	Net Sales proceeds received £m
Property and construction	35	11	2
Total repossessions	**35**	**11**	**2**

Repossessed properties are sold as soon as practicable, with the proceeds applied against outstanding indebtedness.

During the year ended 31 December 2013 the Group disposed of 35 repossessed properties[1]. The total contracted disposal proceeds were adequate to cover the balance outstanding after provisions.

At 31 December 2013, the Group had collateral held as security, as follows:

Repossessed collateral (audited)	**31 December 2013 £m**	31 December 2012 £m
Residential properties	11	30
Commercial property and construction	-	-
Other	-	-
Total	**11**	**30**

[1] The number of properties disposed of during the year ended 31 December 2013 includes those which were subject to an unconditional contract for sale at year end date.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:32 Page 43

2.1 Credit Risk (continued)

Asset quality: Other Financial Instruments

Other financial instruments include available for sale financial assets, derivative financial instruments and loans and advances to banks. Other financial instruments are rated, using external ratings attributed to external agencies, or are assigned an internal rating based on the Parent's internal models, or a combination of both. Mappings to external ratings agencies, in the table below, are therefore indicative only.

Asset quality: **Other financial instruments with ratings equivalent to (audited):**	**31 December 2013** **£m**	31 December 2012 £m
AAA to AA-	1,464	1,222
A+ to A-	203	330
BBB+ to BB-	11,650	25,889
Total	**13,317**	**27,441**

2.1 Credit Risk (continued)

Group Exposures by Country
Set out in the table below is an analysis of the Group's exposure to sovereign debt and other country exposures (primarily financial institution exposure), by selected balance sheet line item, as at 31 December 2013. In addition, for these line items, further information is included on the Group's exposures to selected countries and their associated credit ratings from Standard & Poor's. Further information is included where the Group has an exposure of over £250 million (being with Ireland and the United Kingdom).

31 December 2013 (audited)	**[1]Credit rating**	**[2]Cash and balances £m**	**[3]Loans and advances to Banks £m**	**[4]Available for sale financial assets £m**	**Derivative financial instruments £m**	**Total £m**
Ireland	BBB+	-	11,646	-	4	11,650
Luxembourg	AAA	-	-	-	-	-
United Kingdom	AAA	4,125	994	99	7	5,225
Finland	AAA	-	-	45	-	45
Other		-	184	338	-	522
Total		**4,125**	**12,824**	**482**	**11**	**17,442**

31 December 2012 (audited)	[1]Credit rating	[2]Cash and balances £m	[3]Loans and advances to Banks £m	[4]Available for sale financial assets £m	Derivative financial instruments £m	Total £m
Ireland	BBB+	-	25,885	-	3	25,888
Luxembourg	AAA	-	-	146	-	146
United Kingdom	AAA	6,380	1,198	101	7	7,686
Finland	AAA	-	-	70	-	70
Other		-	7	24	-	31
Total		6,380	27,090	341	10	33,821

Loans and advances to banks in Ireland reduced by 55% during the year from £25.9 billion at 31 December 2012 to £11.6 billion at 31 December 2013. This was as a result of the Group's change in market risk hedging approach from gross flow cash hedging to derivative hedging. Refer to note 13.

[1] *Based on credit ratings from Standard & Poor's.*
[2] *Cash and balances in the United Kingdom primarily consist of amounts placed with the Bank of England (BOE).*
[3] *Loans and advances to banks in Ireland consist primarily of balances with the Group's Parent and balances in the United Kingdom consist primarily of the BOE required collateral for notes in circulation.*
[4] *Available for sale financial assets consist of UK government treasury bills, Finnish government paper and other Supranational bonds.*

2.1 Credit Risk (continued)

Ireland (unaudited) 31 December 2013	0-3 months £m	3-12 months £m	1-2 years £m	Nominal 2-5 years £m	5-10 years £m	Over 10 years £m	Total £m
Loans and advances to banks	615	6,250	2,417	1,677	675	12	11,646
Total	**615**	**6,250**	**2,417**	**1,677**	**675**	**12**	**11,646**

31 December 2012 (unaudited)	0-3 months £m	3-12 months £m	1-2 years £m	2-5 years £m	5-10 years £m	Over 10 years £m	Total £m
Loans and advances to banks	13,570	6,518	2,673	2,346	766	12	25,885
Total	13,570	6,518	2,673	2,346	766	12	25,885

United Kingdom (unaudited) 31 December 2013	0-3 months £m	3-12 months £m	1-2 years £m	Nominal 2-5 years £m	5-10 years £m	Over 10 years £m	Total £m
Cash and balances at Central Banks	4,125	-	-	-	-	-	4,125
Loans and advances to banks	994	-	-	-	-	-	994
Available for sale financial assets[1]	1	-	-	98	-	-	99
Total	**5,120**	**-**	**-**	**98**	**-**	**-**	**5,218**

31 December 2012 (unaudited)	0-3 months £m	3-12 months £m	1-2 years £m	2-5 years £m	5-10 years £m	Over 10 years £m	Total £m
Cash and balances at Central Banks	6,380	-	-	-	-	-	6,380
Loans and advances to banks	1,198	-	-	-	-	-	1,198
Available for sale financial assets[1]	-	-	-	101	-	-	101
Total	7,578	-	-	101	-	-	7,679

As set out in the Group's accounting policies on pages 70 to 89, the Group accounts for each of these assets as follows:

- available for sale financial assets are carried in the balance sheet at their fair value. Other than in respect of impairment, any change in fair value is treated as a movement in the available for sale (AFS) reserve in stockholder's equity; and
- loans and advances to banks and cash and balances at Central Banks are held at amortised cost.

[1] *Measured at fair value*

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:32 Page 46

2.2 Credit Risk Methodologies (audited)

Loan Loss Provisioning Methodology
Through its on-going credit review processes, the Group seeks to identify deteriorating loans early, with a view to taking corrective action to prevent the loan becoming impaired. Loans that are at risk of impairment are managed by dedicated specialist units / debt collection teams, focused on 'work out'.

The identification of loans for impairment assessment as impaired is driven by the Group's credit risk rating systems. For those loans that become impaired, the focus is to minimise the loss that the Group will incur from the impairment. This may involve entering into restructuring arrangements, or action to enforce security, or legal pursuit of individuals who are personally liable for the loan.

All credit exposures, either individually or collectively, are regularly reviewed for objective evidence of impairment. Where such evidence of impairment exists, the exposure is measured for an impairment provision. The criteria used to determine if there is objective evidence of impairment include:

- delinquency in contractual payments of principal or interest;
- cash flow difficulties;
- breach of loan covenants or conditions;
- deterioration of the borrower's competitive position;
- deterioration in the value of collateral;
- external rating downgrade below an acceptable level;
- initiation of bankruptcy proceedings; and
- a request from a borrower for forbearance for reasons of financial stress or distress.

The following factors are also taken into consideration when assessing whether a loss event has occurred at the balance sheet date that may lead to recognition of impairment losses:

Residential Mortgages and Consumer Lending
- debt service capacity; and
- repayment arrears.

Non-property SME and corporate
- debt service capacity;
- financial performance;
- adverse movements in net worth; and
- future prospects.

Property and construction
- debt service capacity and the nature and degree of protection provided by cash flows; and
- the value of any underlying collateral.

Loans with a specific impairment provision attaching to them, together with loans (excluding residential mortgages) which are more than 90 days in arrears or which meet any other impairment criteria are included as impaired loans.

Where objective evidence of impairment exists, as a result of one or more past events, the Group is required to estimate the recoverable amount of the exposure(s).

For financial reporting purposes, loans on the balance sheet, that become impaired, are written down to their estimated recoverable amount. The amount of this write down is taken as an impairment charge to the income statement.

The Group's impairment provisioning methodologies are compliant with International Financial Reporting Standards (IFRS).

IAS 39, Financial Instruments: Recognition and Measurement, requires that there is objective evidence of impairment, and that the loss has been incurred. IAS 39 does not permit the recognition of expected losses, no matter how likely these expected losses may appear. All exposures are assessed for impairment, either individually or collectively.

Methodology for Individually Assessing Impairment
An individual impairment assessment is performed, for any exposure for which there is objective evidence of impairment, and where the exposure is above an agreed minimum threshold. The carrying amount of the exposure, net of the estimated recoverable amount (and thus the specific provision required), is calculated using a discounted cash flow analysis. This calculates the estimated recoverable amount as the present value of the estimated future cash flows, discounted at the exposure's original effective interest rate (or the current effective interest rate for variable rate exposures). The estimated future cash flows include forecasted principal and interest payments (not necessarily contractual amounts due), including cash flows, if any, from the realisation of collateral / security held, less realisation costs.

Methodology for Collectively Assessing Impairment
Where exposures fall below the threshold for individual assessment of impairment, such exposures, with similar credit risk characteristics (e.g. the Group's credit card lending portfolio), are pooled and are collectively assessed for impairment. A provision is then calculated by estimating the future cash flows of the exposures, that are collectively evaluated for impairment. This estimation considers the expected contractual cash flows of the exposures in a portfolio, and the historical loss experience for exposures with credit risk characteristics similar to those in the portfolio being assessed. Assumptions and parameters used to create the portfolio provision, which are based on historical experience (i.e. amount and timing of cash flows / loss given default), are regularly compared against current experience in the loan book and current market conditions.

2.2 Credit Risk Methodologies (continued) (audited)

Where there is objective evidence of impairment on a collective basis, this is reported as a specific provision, in line with individually assessed loans.

Methodology for establishing incurred but not reported (IBNR) provisions
Impairment provisions are also recognised for losses not specifically identified, but which, experience and observable data indicate, are present in the portfolio at the date of assessment. These are described as IBNR provisions. Statistical models are used to determine the appropriate level of incurred but not reported provisions. These models estimate latent losses, taking into account three observed and / or estimated factors:

- loss emergence rates (based on historic grade migration experience or probability of default);
- the emergence period (historic experience adjusted to reflect the current conditions and the credit management model); and
- loss given default rates (loss and recovery rates using historical loan loss experience, adjusted where appropriate to reflect current observable data).

Methodology for loan loss provisioning and Forbearance
Forbearance will always be a trigger event for the Group to undertake an assessment of the customer's financial circumstances and ability to repay. This assessment to determine if impairment has occurred, and if a specific provision is required, will always take place prior to any decision to grant a concession to the customer.

Individually Assessing Impairment and Forbearance
The methodology for individually assessing impairment, whether an exposure is forborne or not, is as outlined above (i.e. on an individual case-by-case basis). The underlying credit risk rating of the exposure, and ultimately the individual impairment assessment, takes into account the specific credit risk characteristics of the exposure.

Collectively Assessing Impairment and Forbearance
Forborne exposures are pooled together for collective impairment provisioning, including IBNR provision calculations, as detailed above. Assumptions and parameters used to create the portfolio provision(s) take into consideration the historical experience on assets subject to forbearance (e.g. amount and timing of cash flows, cure experience, emergence period etc.), adjusted where appropriate to reflect current conditions, and require the satisfactory completion of a twelve month probation period, while being less than 30 days past due, to be eligible to cure from 'probationary' status. Management adjustments are also applied, as appropriate, where historical observable data on forborne assets may be limited. Impairment provisioning methodologies and provisioning model factors applied to forborne loan pools are reviewed regularly, and revised if necessary, to ensure that they remain reasonable and appropriate and reflective of the credit characteristics of the portfolio being assessed and current conditions. This includes a comparison of actual experience to expected outcome. As previously outlined, during the current year, the collective provisioning model methodologies have been further enhanced for forbearance segmentation, including forbearance treatment type (where relevant), and the differentiation of individual model factors between forborne and non-forborne where statistically relevant.

Provisioning and Forbearance
For Residential mortgages, exposures which are subject to forbearance and have a specific provision are reported as both 'forborne' and 'impaired'. The total provision cover on Residential mortgages that are subject to forbearance is higher than that of the similar Residential mortgage portfolio of exposures which are not subject to forbearance.

Further detail on forbearance strategies and the loans and advances that are subject to forbearance measures at 31 December 2013 is set out on page 31 and page 39 to 40. Forbearance related disclosures are subject to evolving industry practice and regulatory guidance.

Impaired loans review
Irrespective of the valuation methodology applied, it is Group policy to review impaired loans above agreed thresholds quarterly, with the review including a reassessment of the recovery strategy, the continued appropriateness of the valuation methodology and the adequacy of the impairment provision.

Where information is obtained between reviews that impact expected cash flows (e.g. evidence of comparable transactions emerging, changes in local market conditions, etc.), an immediate review and assessment of the required impairment provision is undertaken.

An impaired loan is restored to unimpaired status when the contractual amount of principal and interest is deemed to be fully collectible. Typically, a loan is deemed to be fully collectible based on an updated assessment by the Group of the borrower's financial circumstances. The assessment includes a demonstration of the customer's ability to make payments on the original or revised terms and conditions as may be agreed with the Group as part of a sustainable forbearance arrangement.

An analysis of the Group's impairment provisions at 31 December 2013 is set out on pages 35 to 37 and note 17.

Credit Management Process
Account performance is reviewed periodically, to confirm that the credit grade or probability of default assigned remains appropriate and to determine if impairment has arisen. For consumer and smaller ticket commercial exposures, the review is largely based on account behaviour and is highly automated. Where there are loan arrears, excesses, dormancy

2.2 Credit Risk Methodologies (continued) (audited)

etc., the account is downgraded to reflect the higher underlying risk.

For larger commercial loans, the relationship manager reassesses the risk at least annually (more frequently if circumstances or grade require) and re-affirms or amends the grade (credit and PD grade) in light of new information or changes (e.g. up to date financial information, or changed market outlook). Grade migration and adjusted PD grades are analysed for inclusion in the loss model.

The emergence period is calculated using historical loan loss experience. The range of emergence periods is typically three to nine months.

The loss given default (LGD) is calculated using historical loan loss experience and is adjusted, where appropriate, to apply management's credit expertise to reflect current observable data.

Other factors taken into consideration in estimating provisions include domestic and international economic climates, changes in portfolio risk profile and the effect of any external factors, such as legal or competition requirements. Whilst provisioning is an on-going process, all business units formally review and confirm the appropriateness of their provisioning methodologies and the adequacy of their impairment provisions on a half-yearly basis. Their conclusions are reviewed by the Risk function and BRC.

The Group's provisioning methodology is approved by the CRPC on a half yearly basis. The quantum of the Group's loan loss charge, impaired loan balances, and provisions, are also reviewed by BRC yearly, in advance of providing a recommendation to the Audit Committee.

Methodologies for Valuation of Collateral

The Group uses a number of valuation approaches, depending on use of collateral and data availability. The Group has in place a formal valuation policy. Approaches include:

(1) Indexation - Mortgage Portfolios

Mortgage loan book property values are determined by reference to the original or latest property valuations held indexed to the Nationwide UK house price index. The weighted average indexed LTV for the total residential mortgage loan book is 74% at 31 December 2013. Where cash flows arising from the realisation of collateral held are included in impairment assessments, management typically rely on valuations or business appraisals from independent external professionals.

(2) Formal written valuations from independent external professionals

External valuations are sought in circumstances where there continues to be sufficient transactional evidence and market liquidity to support an expert objective view. External qualified firms, with appropriate knowledge of the particular market, are commissioned to provide formal written valuations, including an assessment of the timeline for disposal, in respect of the property.

(3) Assessed valuations, informed by consultations with external valuers

Given the significant dislocation experienced in property markets, the requirement for sufficient transactional evidence and market liquidity to support a formal written expert view is not always met. Verbal consultations with external valuers, familiar with local market conditions, provide general information on market developments, trends and outlook. These consultations are used to benchmark asset values, and the potential timeline for realisation, and form an element of the estimation of the recoverable amount to be used for impairment provisioning.
In some land and development cases, estimated valuations of undeveloped sites may be expressed on a 'per plot' or 'per acre' basis if there is suitable zoning / planning in place, whereas un-zoned rural land may be assumed to have only agricultural value.

(4) Residual value methodologies

Residual value methodologies are used to estimate the current value of a site or part-completed development, based on a detailed appraisal that assesses the costs (building, funding and other costs) and receipts (forecast sales and / or lettings) associated with bringing a development to completion. The type, size and location of the property asset, and its development potential and marketability, are key factors in this assessment process. The Group may look to some of the other valuation methodologies outlined earlier, e.g. residual value methodologies may look to formal professional valuations, verbal consultations with external professionals, or local market knowledge made available by relevant Group management, in determining the appropriate inputs to this analysis.

The appropriate methodology applied depends, in part, on the options available to management to maximise recovery, which are driven by the particular circumstances of the loan and underlying collateral, e.g. the degree of liquidity and recent transactional evidence in the relevant market segment; the type, size and location of the property asset; and its development potential and marketability. Irrespective of the valuation methodology applied, it is Group's policy to review individually significant impaired loans quarterly, with the review including a reassessment of the recovery strategy, the continued appropriateness of the valuation methodology, and the adequacy of the impairment provision.

Where information is obtained between reviews that impacts expected cash flows (e.g. evidence of comparable transactions emerging, changes in local market conditions, etc.), an interim review and assessment of the required impairment provision is undertaken.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:32 Page 49

3. Financial Risk

Financial risk is split into three sub-categories; liquidity and funding risk, market risk and capital management. The following pages outline the management and measurement of each of these three sub-categories.

3.1 Liquidity and Funding Risk

Key points

- The Group has adhered to its policy to materially fund lending through deposits.
- During 2013 the Group participated in the (BOE) Funding for Lending scheme and at 31 December 2013 held £250 million of Funding for Lending treasury bills, which subsequently were repaid.
- The Group held liquid assets of £4.7 billion, which was significantly in excess of regulatory liquidity requirements and within the Group's internal risk appetite at 31 December 2013. This represented a very prudent liquidity position and a strong platform for growing customer lending in 2014.
- At all times during the current financial year, the Group maintained an appropriate liquidity pool and liquidity position, in line with regulatory guidelines and internal risk appetite requirements.
- The Group's loan to deposit ratio increased from 77% at 31 December 2012 to 86% at 31 December 2013 reflecting the positive impacts of the Group's Balance Sheet efficiency strategy.

Definition (audited)

Liquidity risk is the risk that the Group will experience difficulty in financing its assets and / or meeting its contractual payment obligations as they fall due, or will only be able to do so at substantially above the prevailing market cost of funds.

Liquidity risk arises from differences in timing between cash inflows and outflows. Cash inflows for the Group are driven by, among other things, the maturity structure of loans held by the Group, while cash outflows are primarily driven by outflows from customer deposits and lending origination and acquisition.

Liquidity risk can increase due to the unexpected lengthening of maturities, non-repayment of assets or a sudden withdrawal of deposits.

Funding risk is the risk that the Group does not have sufficiently stable and diverse sources of funding or has an inefficient funding structure.

Liquidity and Funding Risk Management (audited)

The Group has established a liquidity and funding risk management framework, that is aligned to the Group's risk appetite and risk targets, and which is aligned with its overall strategy to be a self-funded business with no sustained funding dependency on the Parent or material dependency on wholesale market funding.

The Liquidity and Funding section of the Risk Appetite statement is set by the Board and is reviewed on an annual basis. It sets out the level of liquidity and funding risk that the Board has deemed as acceptable and the key liquidity and funding metrics that the Group has determined best defines its liquidity and funding risk appetite.

The Group's liquidity and funding risk management framework is designed to ensure that the Group manages and monitors its liquidity and funding position in accordance with the defined liquidity and funding risk appetite statement.

The Group's exposure to liquidity and funding risk is governed by policy approved by BRC and the Board. The operational oversight of this policy is delegated to ALCO, an Executive subcommittee of BRC.

The Group's ILAA sets out how the Group assesses, quantifies and manages the key liquidity and funding risks to which it is exposed, and details the Group's approach to determining the level of internal liquidity resources required to be maintained by the Group, for both business-as-usual and stressed scenarios ranging in severity.

Liquidity and funding management within the Group consists of two main activities:

1. *Tactical liquidity management* - which focus on monitoring current and expected future daily cash flows, to ensure that the Group's liquidity needs can be met. This takes into account the Group's access to unsecured funding;

3.1 Liquidity and Funding Risk (continued)

the liquidity characteristics of its portfolio; available for sale assets that are highly marketable assets; cash balances; and contingent assets that can be realised quickly to cover any unforeseen cash outflows; and

2 *Structural liquidity management* - which focuses on assessing the optimal balance sheet structure on both a short term and long term basis taking account of the behavioural and contractual maturity profile of assets and liabilities.

Liquidity and Funding Risk Measurement (audited)

A number of measures are used by the Group to monitor and manage liquidity and funding risk including ratios, deposit outflow triggers, liquidity triggers, stress scenarios and early warning indicators.

Liquidity risk is measured using stress testing and scenario analysis. The Group runs a number of internal liquidity stress scenarios aligned to PRA prescribed stress scenarios; a market-wide stress event; a Group specific stress event and a combination of market-wide and idiosyncratic stress events. These stress scenarios are also performed across a number of outflow time bands. The cash outflows resulting from the stress scenarios are compared against the stock of liquid resources within each maturity band, as defined in the risk appetite statement. Under normal market circumstances the Group must have a liquidity pool available which will be in excess of 100% of the stressed outflows from all stress scenarios performed.

Funding risk is measured by applying and monitoring specific metrics that determine the amount of on-going new retail deposit acquisitions required to fund the Group's asset base across various maturity categories.

The Group has maintained an appropriate liquidity pool in excess of regulatory and internal requirements, throughout 2013. In addition, it also has a contingency funding plan in place, which documents processes and potential actions that can be put in place, in the event of an unexpected shortfall in liquidity.

Customer Deposits

The Group's funding strategy is focused, in particular, on retail deposit funding, with deposits demonstrating a high degree of stability thus providing an appropriate basis to fund customer lending. The Group operates within an internal maximum limit on customer loan to customer deposit ratio of 100%.

During 2013 the Group reduced its customer deposits by £2.4 billion between 31 December 2012 and 31 December 2013 as part of a Group wide focus on balance sheet efficiency.

£16.2 billion of retail deposits related to Post Office branded deposits which have reduced £2.3 billion (13%) over the year. Deposit retention levels continue to improve as the Post Office branded accounts mature and the Group maintains a competitive product offering.

The Group's loan to deposit ratio, as defined on page 3, increased from 77% at 31 December 2012 to 86% at 31 December 2013, primarily reflecting the positive impacts of the Group's balance sheet efficiency strategy.

Customer accounts (unaudited)	31 December 2013 £m	31 December 2012 £m
BoI branded deposits	2,112	2,395
BoI branded current accounts	2,521	2,324
Post Office branded deposits	16,224	18,556
Total	**20,857**	**23,275**

Liquid Assets

The Group maintains a liquid asset portfolio, comprising cash placements and securities that can be used to raise liquidity, either by sale or through secured funding transactions. The portfolio at 31 December 2013 comprises cash balances with Bank of England, UK government treasury bills, Finnish government paper, multi-lateral development bank bonds and banks placements. The composition of the portfolio is set out below. Interbank placements comprise of both placements with external banks and the Parent. While these placements are considered liquid assets by the Group they are not deemed to be PRA BIPRU eligible liquid assets.

The Group utilises its liquidity stress testing to determine the minimum required level of the liquid asset portfolio and the components thereof.

3.1 Liquidity and Funding Risk (continued)

Composition of the liquid asset portfolio (unaudited)	31 December 2013 £m	31 December 2012 £m
Balances with Central Banks	4,088	6,350
Government bonds	143	146
Other listed securities	339	195
Interbank placements	150	416
Total	**4,720**	**7,107**

At 31 December 2013 £4,570 million of the liquid asset portfolio is PRA BIPRU eligible (31 December 2012: £6,691 million).

Liquidity and Funding Risk Monitoring
The Group's daily, weekly and monthly liquidity reporting, including a comprehensive suite of liquidity early warning triggers, are produced for use by the Group's Treasury function, to assess and manage the Group's current and future liquidity risk position. Daily liquidity reports are reviewed by Treasury, Finance and Risk functions and by the Group's senior management. Liquidity risk reports are also reviewed at ALCO monthly meetings, with actions agreed as appropriate. Liquidity stress test results are also reported to senior management on a daily basis and, for ease of interpretation, make use of both graphs and a series of pre-defined operational triggers which are reported to ALCO, BRC and the Board.

The Group's liquidity position is supported by its liquid asset portfolio, the contingent liquidity collateral available and by the various management actions defined in its Contingency Funding Plan.

Funding risk management is incorporated into the Group's funding plan which is monitored regularly and updated annually.

Placements and borrowings with the Parent are transacted to hedge the Group's market risk exposure and are not relied upon by the Group for liquidity purposes. Furthermore, the Group has in place a contractual Master Netting Agreement with the Parent whereby, in the event of a default by either party, all amounts due or payable will be settled immediately on a net basis. In December 2013 the Group changed the market risk hedging approach to derivative hedging. This approach will gradually replace the gross cash hedging previously performed over time as legacy placements and borrowings with the Parent expire. Therefore the amounts due from and due to the Parent have reduced at the end of 2013 from £25.9 billion and £25.7 billion, respectively at 31 December 2012, to £11.7 billion and £11.7 billion, respectively, at 31 December 2013.

Contingent Liquidity
The Group holds significant contingent liquidity collateral, comprised of mortgage-backed securities issued by Bowbell No 1 plc (refer to note 36), and raw loans prepositioned in the BOE Discount Window Facility. This contingent liquidity collateral is capable of being pledged against borrowings from Central Banks and other external market participants. During the year the Group used a portion of the mortgages available as collateral to drawdown on the BOE Funding for Lending Scheme. £250 million of Funding for Lending Treasury Bills were obtained as a result which the Group held within its liquid asset portfolio as at 31 December 2013.

External Ratings
The Group is rated by both Moody's and Fitch. Given the Group's funding strategy and in particular, its focus on growing and retaining retail deposits as its primary funding mechanism, the direct impact on liquidity risk of movements in the Group's credit rating is limited. See table below for ratings summary:

BoI UK ratings (unaudited)	31 December 2013 £m	31 December 2012 £m
Moody's	Ba1 negative outlook	Ba1 negative outlook
Fitch	BBB stable outlook	BBB stable outlook

3.1 Liquidity and Funding Risk (continued)

Maturity Analysis of Financial Assets and Liabilities

The tables below summarise the contractual maturity profile of the Group's financial assets and liabilities, at 31 December 2013 and 31 December 2012, based on the contractual discounted repayment obligations. The Group does not manage liquidity risk on the basis of contractual maturity, instead the Group manages liquidity risk by adjusting the contractual cash inflows and outflows of the Balance Sheet to reflect them on a behavioural basis. This includes the incorporation of the inherent stability evident in the retail deposit book.

Customer accounts include a number of term accounts that contain access features which allow customers to access a portion of, or all of, their deposit, notwithstanding that this withdrawal could result in a financial penalty being paid by the customer. For such accounts, the portion subject to the potential early access has been classified accordingly in the table below.

31 December 2013 (unaudited)	Repayable on demand £m	Up to 3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Financial Assets						
Cash and balances with Central Banks	4,125	-	-	-	-	4,125
Derivative financial instruments	-	7	3	1	-	11
Loans and advances to banks	196	982	-	-	-	1,178
Loans and advances to banks - related party transactions	598	17	6,250	4,094	687	11,646
Available for sale financial assets	-	71	-	411	-	482
Loans and advances to customers (before impairment provisions)	1,256	1,191	1,505	4,510	10,185	18,647
Total assets	**6,175**	**2,268**	**7,758**	**9,016**	**10,872**	**36,089**
Financial Liabilities						
Deposits from banks	9	-	-	-	-	9
Deposits from banks - related party transactions	636	6	6,255	4,619	135	11,651
Customer accounts	12,445	3,448	3,535	1,429	-	20,857
Derivative financial instruments	-	8	3	-	-	11
Subordinated liabilities	-	-	-	-	658	658
Total liabilities	**13,090**	**3,462**	**9,793**	**6,048**	**793**	**33,186**
Net total assets and liabilities	**(6,915)**	**(1,194)**	**(2,035)**	**2,968**	**10,079**	**2,903**
Cumulative total assets and liabilities	**(6,915)**	**(8,109)**	**(10,144)**	**(7,176)**	**2,903**	**2,903**

3.1 Liquidity and Funding Risk (continued)

31 December 2012 (unaudited)	Repayable on demand £m	Up to 3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Financial Assets						
Cash and balances with Central Banks	6,380	-	-	-	-	6,380
Derivative financial instruments	-	7	3	-	-	10
Loans and advances to banks	324	881	-	-	-	1,205
Loans and advances to banks - related party transactions	11,272	2,298	6,518	5,019	778	25,885
Available for sale financial assets	-	19	-	322	-	341
Loans and advances to customers						
(before impairment provisions)	1,494	1,296	1,341	4,551	10,031	18,713
Total assets	19,470	4,501	7,862	9,892	10,809	52,534
Financial Liabilities						
Deposits from banks	5	-	-	-	-	5
Deposits from banks - related party transactions	1,801	18,940	1,654	3,159	183	25,737
Customer accounts	12,349	10,023	700	203	-	23,275
Derivative financial instruments	-	6	3	-	-	9
Subordinated liabilities	-	-	-	-	658	658
Total liabilities	14,155	28,969	2,357	3,362	841	49,684
Net total assets and liabilities	5,315	24,468	5,505	6,530	9,968	2,850
Cumulative total assets and liabilities	5,315	(19,153)	(13,648)	(7,118)	2,850	2,850

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

3.2 Market Risk

Key points

- The Group does not engage in speculative trading for the purposes of profit-making as a result of anticipation of movements in financial markets. Therefore, no discretionary risk is taken by the Group.
- During 2013, the Group continued to manage interest rate and foreign exchange exposure at acceptable levels, by hedging exposures with its Parent as a counterparty.
- In December 2013 the Group changed its market risk hedging approach from gross cash hedging to net derivatives hedging.

Definition (audited)

Market risk is the risk that changes in the level of interest rates and the movement in exchange rates between currencies and financial instruments will have an adverse financial impact on the Group's cash flows.

Market risk arises, on the asset side of the balance sheet, mainly through fixed rate lending, and on the liability side, through fixed rate deposit products. Market risk can also arise where variable rate assets and liabilities re-price at different frequencies (monthly, quarterly, semi-annually), or where lending re-prices with changes in Bank of England rates, but is funded at short dated market rates. Changes in the differential or basis between different floating rates (such as assets re-pricing at the base rate and liabilities re-pricing at LIBOR) can have an impact on the Group's net interest margin.

Structural interest rate risk arises from the existence of non-interest bearing liabilities (principally equity and non-interest bearing current accounts less fixed assets) on the balance sheet. If these net liabilities were used to fund variable rate assets, the Group's earnings would be exposed to variation in interest rates.

Market Risk Management (audited)

The market risk appetite is set by the Board and is reviewed on an annual basis. The Board delegates responsibility of the monitoring of market risk limits to ALCO, which has primary responsibility for the oversight of market risk within the confines of the Risk Appetite limits set by the Board.

The Group has no risk appetite for the holding of proprietary market risk positions or the running of open banking book market risk exposures. The Group, therefore, has no proprietary trading book. The Group does have customer derivative foreign exchange (FX) forward contracts, which are considered held for trading, as hedge accounting is not applied. These transactions are hedged with the Parent.

The Group manages its interest rate risk position through arrangements with the Parent. Prior to December 2013 the hedging approach performed was on a cash basis, whereby all monies received from customer deposits were placed onward with the Parent for an equivalent term and re-pricing frequency, and customer lending was funded via amounts borrowed from the Parent on an equivalent term and re-pricing frequency basis. In December 2013 the Group amended the market risk hedging approach to incorporate the use of derivative contracts as an appropriate hedging instrument. The overall market risk hedging approach from December 2013 is prioritised as follows; (i) seek to naturally hedge within the Balance Sheet, (ii) execute derivative hedging contracts with the Parent or (iii) execute gross cash hedges. Therefore, over time the cash hedging deals with the Parent will be replaced by derivative contracts. Derivatives will be executed with the Parent only and are subject to an ISDA and CSA. Collateral requirements are calculated daily and posted as required. The Group uses derivatives for hedging purposes only and seeks to apply hedge accounting where possible. The Group continues to maintain a de-minimis limit for interest rate risk to reflect operational requirements only. This limit is reviewed and approved by BRC.

The Group's lending and deposits are almost wholly (>95%) denominated in sterling. Any foreign currency transactions are hedged to acceptable levels with the Parent.

3.2 Market Risk (continued)

It is the Group's policy to manage structural interest rate risk, by investing its net non-interest bearing liabilities in a portfolio of fixed rate assets, with an average life of 3.5 years and a maximum life of 7 years.

Market Risk Measurement and Sensitivity (audited)

The Group's interest rate risk position is measured and reported, daily. The daily interest rate risk position is calculated by establishing the contractual re-pricing behaviour of assets, liabilities and off-balance sheet items on the Group's balance sheet, before modelling these cash flows and discounting them at current yield curve rates. Certain behavioural assumptions to reflect expected asset prepayment, are overlaid for interest rate sensitive assets and liabilities These behavioral assumptions are back-tested on a monthly basis and updated as necessary.

The impact on the Group's net margin for one year, ahead of an immediate and sustained 50 basis points shift, up or down, in the sterling yield curve applied to the Banking book at 31 December 2013, is as follows:

(Audited)	**Year ended 31 December 2013 £m**	Year ended 31 December 2012 £m
+ 50 basis points	0.33	0.06
- 50 basis points	(0.33)	(0.06)

The above sensitivity is indicative of the magnitude and direction of exposures but requires qualification, in that the results are based on an immediate and sustained shift of the same magnitude across the yield curve.

3.3 Capital Management

Key points

- Effective capital management is critical to the Group's ability to manage its businesses, grow organically and achieve its strategy.
- The Group operates a robust capital management framework in accordance with its capital management policy.
- The Group has complied with all its regulatory requirements throughout 2013.

Capital Management Objectives and Policies (audited)
The objectives of the Group's capital management policy are to, at all times, comply with regulatory capital requirements, and to ensure that the Group has sufficient capital to cover the risks of its business and support its strategy. Capital adequacy and its effective management is critical to the Group's ability to operate its businesses, to grow organically and to pursue its strategy. The Group's business and financial condition could be affected if it is not able to manage its capital effectively or if the amount of capital is insufficient due to a materially worse than expected financial performance (including, for example, reductions in profits and retained earnings as a result of impairment losses or write downs, increases in risk weighted assets and delays in the disposal of certain assets as a result of market conditions).

Capital Resources
The Group manages its capital resources to ensure that the overall level of resources exceeds the Group's capital requirements. The Group's capital requirements are primarily driven by credit risk (including credit concentration risk) and operational risk. The Group's capital requirements also incorporate a regulatory capital planning buffer, the size of which is determined by stress testing as part of the ICAAP process.

The Group regularly assesses its existing and future capital adequacy under a range of scenarios, using a combination of quantitative and qualitative analyses in the ICAAP, which is reviewed by the regulator on a periodic basis. The ICAAP, which acts as a link between the Group's strategy, capital and risk, is approved annually by the Board.

Capital Requirements
The Group has complied with its regulatory capital requirements throughout 2013.

In December 2013, the PRA issued guidance on the UK implementation of Basel III. The Group is currently assessing the potential requirement to alter the amount and structure of its capital base to ensure ongoing compliance.

The Group's Pillar 3 disclosures can be accessed on the Parent's website.

Group capital resources (audited)	**31 December 2013 £m**	31 December 2012 £m
Equity (including other equity reserves)	1,233	1,054
Preference stock	300	300
Subordinated loan capital	658	658
Total capital resources	**2,191**	**2,012**

Capital resources disclosed are audited accounting capital resources. Regulatory Capital disclosures on a Basel II and Basel III are included on pages 15 to 18 of the Strategic Report.

In the year ended 31 December 2013, the Group's total capital resources increased by £179 million, primarily due to:

- a positive movement in reserves of £58 million;
- the issuance of £35 million in additional ordinary stock to the Group's Parent; and
- a capital contribution of £86 million.

Governance

Directors and Other Information

Chairman	Mr. Christopher Fisher (N) (RE)
Non-Executive Directors	Ms. Laurel Powers-Freeling (A) (N) (RI) (RE) Mr. Patrick Haren (N) (RE) Mr. Senan Murphy Mr. Peter Shaw (A) (RI) Mr. David Bennett (A) (RI)
Executive Directors	Mr. Desmond Crowley Mr. David McGowan Mr. Stephen Matchett

(A) Members of the Audit Committee
(N) Members of the Nomination Committee
(RI) Members of the Risk Committee
(RE) Members of the Remuneration Committee.

Company Secretary
Hill Wilson Secretarial Ltd

Registered Office
Bow Bells House,
1 Bread Street,
London,
EC4M 9BE

Registered Number
07022885

Independent Auditors
PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
7 More London Riverside,
London,
SE1 2RT

Directors and other Information (continued)

Board of Directors serving at the date of signing

Chairman

Christopher Fisher (60)
Appointed Chairman in June 2012, having served as an independent Non-Executive Director since March 2010. Chair of the Nomination Committee and a member of the Remuneration Committee. Over 30 years of corporate finance experience, principally at Lazard, where he became a Managing Director, subsequently at KPMG, where he was Vice Chairman, (Corporate Finance), and most recently at Penfida, the financial adviser to pension scheme trustees, where he was a Senior Partner and now serves as a Senior Adviser. Other current appointments include serving as a Non-Executive Director of Segro, the FTSE 200 property company, and as Chairman of the governing body of the University of Reading.

Chief Executive Officer

Desmond Crowley, BA (Mod) Econ, FCMA (54)
Joined Bank of Ireland Group in 1988. In March 2000, became a member of the Group Executive Committee, on being appointed Chief Executive of Retail Banking Ireland. Appointed Chief Executive of UK Financial Services, Director of Bristol & West plc and Bank of Ireland UK Holdings plc in January 2006. Appointed Director of the Parent in October 2006, until his retirement from this position in June 2011. Appointed as Chief Executive Officer – Retail (Ireland & UK) in May 2009 and Chief Executive - Retail UK Division in March 2012. A Director of First Rate Exchange Services, the foreign exchange joint venture with UK Post Office. He is also a Director of New Ireland Assurance Company plc.

Executive Directors

David McGowan, LLB (58)
Appointed Director of Bank of Ireland (UK) plc in September 2009. Having initially served as Chief Executive Officer (CEO), David was appointed Chief Risk Officer in October 2012. David joined Bank of Ireland Group in 1979 and has held various executive positions including a member of the Group Credit Committee. David has been a Director of a number of companies in the Group and held other senior management positions including CEO Northern Ireland (1998 - 2002) and CEO Business Banking UK (2002 - 2009). Appointed Director of Bristol & West plc and Bank of Ireland UK Holdings plc in February 2005 and appointed to the Board of Directors of NIIB Group Limited in January 2012.

Stephen Matchett, BSc, FCA (45)
Appointed Director and Chief Financial Officer, Bank of Ireland (UK) plc, in March 2010. Stephen joined Bank of Ireland in 2001 having previously worked for PricewaterhouseCoopers and Deloitte. Since joining Bank of Ireland, he has held a number of management positions, including Finance Director of Bank of Ireland Northern Ireland and subsequently Business Banking UK and Chief Operating Officer of Business Banking UK. Stephen is a Director of a number of companies within the Bank of Ireland Group, including Bristol & West plc (appointed November 2009) and Bank of Ireland UK Holdings plc (appointed November 2009). Stephen is also a Director of NIIB Group Limited, Bank of Ireland Trustee Company Limited and First Rate Enterprise Services Limited.

Directors and Other Information (continued)

Independent Non-Executive Directors

Laurel Powers-Freeling, BA, MSc (56)
Appointed Director of Bank of Ireland (UK) plc in April 2010. Chair of the Audit Committee and member of the Risk, Remuneration and Nomination Committees. Non-Executive Director of C Hoare & Co Private Bank, Findel plc, ACE European Group, Premium Credit Limited and Governor of the Royal Academy of Music. Former Director of the Bank of England, UK Country Manager of American Express Services Europe Ltd, Group Executive Director of Marks & Spencer Group plc, Chief Executive of Marks & Spencer Financial Services plc and Managing Director – Wealth Management Division of Lloyds TSB Group plc.

Peter Shaw BA, ACIB, DipFS, FCIOBS (54)
Appointed Director of Bank of Ireland (UK) plc in January 2013. Chair of the Risk Committee and member of the Audit Committee. He has formerly held a variety of senior executive positions, most recently as Interim Chief Risk Officer of the Co-operative Banking Group, and prior to that within Royal Bank of Scotland Group and NatWest where he was Chief Risk Officer for the Retail, Wealth and Ulster businesses. Peter has a wide range of experience in both Risk and Business roles throughout a career in Financial Services of over 30 years.

David Bennett, MA (Econ) (52)
Appointed Director of Bank of Ireland (UK) plc in February 2013. Member of the Risk Committee and Audit Committee. David is currently Chairman of the Audit Committee and Finance Committee of easyJet plc and a Non Executive Director of a number of both listed and unlisted international companies. David has previously held various executive positions as Chief Executive Officer, Finance Director and Executive Director at various financial services institutions including Abbey National plc, Alliance and Leicester plc, Lloyds TSB Group and Cheltenham and Gloucester plc.

Group Nominated Non-Executive Directors

Senan Murphy BComm, FCA (45)
Appointed Director of Bank of Ireland (UK) plc in June 2012. Head of Group Manufacturing, responsible for Group-wide operations and technology. Formerly Chief Operating Officer and Finance Director at Ulster Bank, which he joined in 2008. Previously he was Chief Financial Officer of Airtricity, whose sale to Scottish and Southern Energy, he led in 2007. Before that, Senan worked in a number of senior roles in General Electric in both the US and Europe.

Patrick Haren (63)
Appointed Director of Bank of Ireland (UK) plc in June 2012. Chair of the Remuneration Committee and a member of the Nomination Committee. Patrick joined Northern Ireland Electricity (NIE) as Chief Executive in 1992 and took the company through privatisation. He later became Group Chief Executive of Viridian Group plc, as part of the restructuring of NIE which he led in 1998. Patrick led the enlarged group to become a leading FTSE 250 company, employing over 1,600 staff, before overseeing the sale of the business to Arcapita in 2006. Between 2007 and 2012 Patrick served as Deputy Chairman and Chairman of Viridian Group. He was awarded a knighthood in 2008 for services to the electricity industry in Northern Ireland. He was appointed to the Court of Directors of the Bank of Ireland Group in January 2012.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 60

Report of the Directors

The Directors of Bank of Ireland (UK) plc present their consolidated audited report and financial statements for the year ended 31 December 2013. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the EU in accordance with the provisions of the Companies Act 2006. Directors are listed in the Governance section on pages 57 to 59. The future developments of the Group are incorporated in the Strategic Report in section 1.4

Principal Activities

The Bank is an 'authorised institution' under the Financial Services and Markets Act 2000 and is regulated by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA). The principal activities of the Group are the provision of an extensive range of banking and other financial services in Great Britain and Northern Ireland.

Financial Performance

The Group's profit attributable to the owners of the Parent, for the year ended 31 December 2013, was £61 million (for the year ended 31 December 2012: £92 million loss). There was no profit or loss attributable to non-controlling interests for the year ended 31 December 2013, (year ended 31 December 2012: £2 million). An analysis of performance is set out in the Strategic Report on pages 9 to 19.

Dividends

On 31 March 2013 the second non-cumulative preference dividend fell due; this was not paid as the terms and conditions were not met. The Directors do not recommend the payment of a dividend on the ordinary shares in respect of this financial year.

Board Membership

The following Directors were appointed during the year and up to the date of signing:

- Peter Shaw, Non-Executive, 1 January 2013; and
- David Bennett, Non-Executive, 7 February 2013.

The following Director retired during the year:

- Robert Walker, Non-Executive, 28 March 2013.

Corporate Governance

It is the Group's policy not to include the disclosures in respect of voluntary corporate governance codes of practice, as it is a wholly owned subsidiary of The Governor and Company of the Bank of Ireland, a company incorporated by charter in the Republic of Ireland. The Consolidated Annual Report of the Bank of Ireland Group details the Corporate Governance framework applicable to the Group and its subsidiaries. Bank of Ireland Group financial statements are available on www.bankofireland.com or at Bank of Ireland, Head Office, 40 Mespil Road, Dublin 4.

Corporate Responsibility

The Group strives to make a positive contribution to the economy by supporting our customers and investing in the communities in which we operate. The Group participates in a number of Parent initiatives including Give Together, a community giving initiative under which employees are supported in raising money and volunteering days for good causes. The Parent is also conscious of its impact on the environment and has taken steps to reduce energy consumption at high usage locations that provide services to the Group.

Risk Management

The Group's principal risks and uncertainties are discussed in the Strategic Report on pages 20 to 22.

Employees

At 31 December 2013, the Group has 135 direct employees (for the year ended December 2012: 135 direct employees) and 245 employees (for the year ended 31 December 2012: 160 employees) who work under long-term secondment arrangements from the Parent.

The Group is committed to employment practices and policies, which recognise the diversity of the Group's workforce and are based on equal opportunities for all employees. In either recruitment or employment practices, the Group does not discriminate against individuals on the basis of any factor which is not relevant to performance including individuals' sex, race, colour, disability, sexual orientation, marital status or religious beliefs.

Report of the Directors (continued)

The Group has a number of programmes to support colleagues who become disabled or acquire a long-term health condition, which include, but are not limited to, workplace adjustments to provide physical equipment or alteration to the way a job is done. Should a disabled person find that they are unable to continue to function in their existing role, the Group will provide an alternative role, facilitating appropriate retraining.

To support continued employment and training, career development and promotion of all employees, including disabled persons, the Group provides a suite of learning and development activities which are facilitated in conjunction with the Parent. Through the Group's ongoing employee performance monitoring and appraisal process, incorporating frequent line manager and employee discussions, individual employees are encouraged and supported to pursue their own personal development.

The Group also endeavours to ensure that employees are provided with information on matters of concern to them and encourages active involvement of employees to ensure that their views are taken into account in reaching decisions. To facilitate this, there is regular consultation with employees or their representatives, through regular meetings, bulletins and the use of the Group's intranet, which provides a flexible communication channel for employees.

Political Donations
No political donations were made during the year ended 31 December 2013 or in the year ended 31 December 2012.

Going Concern
The Directors have considered the appropriateness of the going concern basis in preparing the financial statements, for the year ended 31 December 2013, on pages 71 and 72 which form part of the Report of the Directors.

Books of Account
The Directors ensure that proper books and accounting records are kept at the Group's registered office, through the appointment of suitably qualified competent personnel, the implementation of appropriate computerised systems and the use of financial and other controls over the systems and the data.

Third Party Indemnity Provision
A qualifying third party indemnity provision (as defined in Section 234 of the Companies Act 2006) was and remains in force for the benefit of all Directors of the Group and former Directors who held office during the year. The indemnity is granted under article 137 of the Bank's Articles of Association.

Post Balance Sheet Events
These are described in note 38 to the consolidated financial statements.

By order of the Board

Stephen Matchett
Director
5 March 2014
Company Number: 07022885

Statement of Directors' Responsibilities

The Directors are responsible for preparing the annual report and the consolidated financial statements in accordance with applicable law and regulations.

UK company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors have prepared the Group's and the Bank's financial statements, in accordance with International Financial Reporting Standards (IFRSs) and International Financial Reporting Interpretations Committee (IFRIC) interpretations, as adopted by the European Union. In preparing these financial statements, the Directors have also elected to comply with IFRSs, issued by the International Accounting Standards Board (IASB). The financial statements have been prepared under the historical cost convention, as modified to include the fair valuation of certain financial instruments.

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 state of affairs of the Group and Bank and of the profit or loss of the Group for that period.

In preparing these financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether applicable International Financial Reporting Standards (IFRSs), as adopted by the European Union, have been followed, subject to any material departures being disclosed and explained in the financial statements; and
- Prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy, at any time, the financial position of the Bank and Group and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Audit confirmation

In accordance with Section 418, the Directors Report shall include a statement in the case of each Director in office at the date the Director's report is approved, that:

(a) So far as the Director is aware, there is no relevant audit information of which the Group's auditors are unaware; and

(b) He / she has taken all the steps that 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 Group's auditors are aware of that information.

By order of the Board
For and on behalf of Bank of Ireland (UK) plc

Stephen Matchett
Director
5 March 2014
Company Number: 07022885

Independent Auditors' Report

We have audited the Group financial statements of Bank of Ireland (UK) plc for the year ended 31 December 2013 which comprise the Consolidated Income Statement, the Consolidated Statement of Other Comprehensive Income, the Consolidated Balance Sheet, the Consolidated Statement of Changes in Equity, the Consolidated Cash Flow Statement, the Group Accounting Policies and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective responsibilities of directors and auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 62, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Group's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the Group financial statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2013 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Report of the Directors for the financial year for which the Group financial statements are prepared is consistent with the Group financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Other matter

We have reported separately on the separate financial statements of Bank of Ireland (UK) plc for the year ended 31 December 2013, this can be found on page 134 of the Bank financial statements.

Hamish Anderson (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
5 March 2014

Consolidated Financial Statements

Consolidated Income Statement
for the year ended 31 December 2013

	Notes	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Interest income	2	1,101	1,305
Interest expense	3	(686)	(1,042)
Net interest income		**415**	**263**
Fee and commission income	4	118	142
Fee and commission expense	4	(112)	(107)
Net trading income	5	-	2
Other operating income	6	1	(7)
Total operating income		**422**	**293**
Operating expenses	7	(274)	(272)
Operating profit before impairment charges on financial assets		**148**	**21**
Impairment charges on financial assets	9	(125)	(183)
Operating profit / (loss)		**23**	**(162)**
Share of profit after tax of jointly controlled entity	10	34	32
Profit / (loss) before taxation		**57**	**(130)**
Taxation credit	11	4	38
Profit / (loss) for the year		**61**	**(92)**
Attributable to non-controlling interests		-	(2)
Attributable to owners of the Parent		61	(90)
Profit / (loss) for the year		**61**	**(92)**

Consolidated Statement of Other Comprehensive Income
for the year ended 31 December 2013

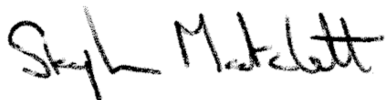
	Notes	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Profit / (loss) for the year		**61**	**(92)**
Other comprehensive income, net of tax:			
Net change in available for sale reserve (net of tax)[1]	15	(4)	-
Total items that may be reclassified to profit or loss in subsequent periods		**(4)**	**-**
Net actuarial gain / (loss) on defined benefit schemes	25	1	(1)
Total items that will not be reclassified to profit or loss in subsequent periods		**1**	**(1)**
Other comprehensive income / (expense) for the year, net of tax		**(3)**	**(1)**
Total comprehensive income / (expense) for the year, net of tax		**58**	**(93)**
Total comprehensive income attributable to owners of the Parent		58	(91)
Total comprehensive income attributable to non-controlling interests		-	(2)
Total comprehensive income / (expense) for the year, net of tax		**58**	**(93)**

[1] *Net of tax of £1 million*

Consolidated Balance Sheet
as at 31 December 2013

	Notes	31 December 2013 £m	31 December 2012 £m
Assets			
Cash and cash equivalents	12	4,125	6,380
Items in the course of collection from other banks		182	193
Derivative financial instruments	13	11	10
Loans and advances to banks	14	12,824	27,090
Available for sale financial assets	15	482	341
Loans and advances to customers	16	17,928	18,018
Interest in jointly controlled entity	18	55	54
Intangible assets	19	46	52
Current tax asset		4	1
Other assets	20	110	133
Deferred tax asset	26	128	74
Total assets		**35,895**	**52,346**
Equity and liabilities			
Deposits from banks	21	11,660	25,742
Customer accounts	22	20,857	23,275
Items in the course of transmission to other banks		94	173
Derivative financial instruments	13	11	9
Other liabilities	23	1,058	1,100
Provisions	24	24	22
Retirement benefit obligation	25	-	2
Current tax liability		-	11
Subordinated liabilities	27	658	658
Total liabilities		**34,362**	**50,992**
Equity			
Share capital	29	1,151	1,116
Retained earnings		(1)	(63)
Other reserves		383	301
Total equity attributable to owners of the Parent		**1,533**	**1,354**
Total equity and liabilities		**35,895**	**52,346**

The financial statements on pages 64 to 132 were approved by the Board on 5 March 2014 and were signed on its behalf by:



Stephen Matchett
Director
5 March 2014
Company Number: 07022885

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

Consolidated Statement of Changes in Equity for the year ended 31 December 2013

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Share capital		
Balance at 1 January	1,116	1,056
Issue of share capital – ordinary	35	60
Balance at 31 December	**1,151**	**1,116**
Retained earnings		
Balance at 1 January	(63)	(2)
Initial reserves on consolidation	-	3
Profit / (loss) for the year attributable to equity holders of the Parent	61	(90)
Purchase of non-controlling interest[1]	-	27
Net actuarial gain / (loss) on defined benefit schemes	1	(1)
Balance at 31 December	**(1)**	**(63)**
Other reserves:		
Available for sale reserve		
Balance at 1 January	1	1
Changes in fair value	(5)	-
Deferred tax on reserve movements	1	-
Balance at 31 December	**(3)**	**1**
Capital contribution		
Balance at 1 January	300	300
Contribution during period	86	-
Balance at 31 December	**386**	**300**
Total other reserves	**383**	**301**
Total equity	**1,533**	**1,354**
Non-controlling interest		
Balance at 1 January	-	24
Capital contribution by non-controlling interest	-	11
Loss for the year attributable to non controlling interest	-	(2)
Purchase of non-controlling interest[1]	-	(33)
Balance at 31 December	**-**	**-**
Total equity	**1,533**	**1,354**
Included in the above:		
Total comprehensive income attributable to owners of the Parent	58	(91)
Total comprehensive income attributable to non-controlling interest	-	(2)
Total comprehensive income for the year	**58**	**(93)**

[1] In 2012, the Group signed an agreement to enhance its strategic partnership with the UK Post Office. Prior to this transaction, the Group held 50.01% of the equity of Midasgrange Limited with the remaining 49.99% held by the UK Post Office. As a consequence of this agreement in 2012, the Group purchased this non-controlling interest for total consideration of £6 million and recognised a gain of £27 million in retained earnings.

Consolidated Cash Flow Statement
for the year ended 31 December 2013

	Notes	**Year ended 31 December 2013 £m**	Year ended 31 December 2012 £m
Cash flows from operating activities			
Profit / (loss) before tax		57	(130)
Interest expense on subordinated liabilities and other capital instruments	3	52	45
Depreciation and amortisation	7,15	9	8
Impairment charges on loans and advances to customers	9	125	183
Share of results of associates and jointly controlled entities	10	(34)	(32)
Net change in prepayments and interest receivable	20	18	71
Net change in accruals and interest payable	23	(101)	27
Retirement benefit obligation	25	1	(1)
Charge for provisions	24	17	22
Cash flows from operating activities before changes in operating assets and liabilities		**144**	**193**
Net change in items in the course of collection from the banks		(68)	18
Net change in derivative financial instruments	13	1	(1)
Net change in loans and advances to banks	14	1,284	299
Net change in loans and advances to customers	16	(35)	(2,828)
Net change in other assets	20	4	(9)
Net change in deposits from banks	21	(14,082)	2,147
Net change in customer accounts	22	(2,418)	2,086
Net change in other liabilities	23	59	(53)
Net change in provisions	24	(15)	-
Net change in retirement benefit obligation	25	(2)	-
Net cash flow from operating assets and liabilities		**(15,272)**	**1,659**
Net cash flow from operating activities before taxation		**(15,128)**	**1,852**
Taxation refunded / (paid)		24	(21)
Net cash flow from operating activities		**(15,104)**	**1,831**
Investing activities (section a - see below)		(116)	2,019
Financing activities (section b - see below)		(17)	147
Net change in cash and cash equivalents		**(15,237)**	**3,997**
Opening cash and cash equivalents		21,155	17,158
Closing cash and cash equivalents	12	**5,918**	**21,155**

Consolidated Cash Flow Statement
for the year ended 31 December 2013 (continued)

	Notes	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
(a) Investing activities			
Additions to available for sale financial assets	15	(167)	(360)
Redemptions of available for sale financial assets	15	19	280
Disposal of available for sale financial assets	15	-	1,282
Dividends received from jointly controlled entities	18	33	40
Additions to intangible assets	19	(3)	(2)
Disposal of intangible assets	19	2	1
Net cash and cash equivalents acquired from common control transactions	37	-	778
Cash flows from investing activities		**(116)**	**2,019**
(b) Financing activities			
Issue of share capital	29	35	60
Consideration paid in respect of purchase of NIIB		-	(8)
Consideration paid in respect of purchase of non controlling interest		-	(6)
Capital contribution by non controlling interest		-	11
Interest paid on subordinated liabilities	3	(52)	(45)
Issue of new subordinated liabilities	27	-	135
Cash flows from financing activities		**(17)**	**147**

Group Accounting Policies

Index

	Page
Accounting policies	70
Basis of preparation	70
Adoption of new accounting standards	70
Comparatives	71
Going concern	71
Group financial statements	72
Foreign currency translation	74
Interest income and expense	74
Fee and commission income and expense	75
Operating profit / loss	75
Leases	75
Financial assets	75
Financial liabilities	77
Valuation of financial instruments	77
Sale and repurchase agreements	78
Derivative financial instruments and hedge accounting	78
Impairment of financial assets	79
Property, plant and equipment	81
Intangible assets	81
Provisions	82
Employee benefits	82
Income taxes	83
Cash and cash equivalents	84
Share capital and reserves	84
Offsetting financial instruments	84
Collateral	84
Financial guarantees	85
Operating segments	85
Materiality	85
Impact of new accounting standards	86
Critical accounting estimates and judgements	88

Accounting Policies

The following are the principal accounting policies for the Bank of Ireland (UK) plc Group and Bank.

Basis of preparation

The financial statements comprise the Consolidated and Bank income statements, the Consolidated and Bank statements of other comprehensive income, the Consolidated and Bank balance sheets, the Consolidated and Bank statements of changes in equity, the Consolidated and Bank cash flow statements, the Group and Bank accounting policies, the notes to the Consolidated financial statements and the notes to the Bank financial statements. The notes include the information contained in those parts of sections 2.1, 2.2, 3.1, 3.2 and 3.3 of the Risk Management Report, that are described as being an integral part of the financial statements.

The financial statements have been prepared on the going concern basis, in accordance with International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRIC) interpretations, as adopted for use in the European Union and as applied in accordance with the provisions of the Companies Act 2006.

The financial statements have been prepared under the historical cost convention, as modified to include the fair valuation of certain financial instruments.

The preparation of the financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting year. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. A description of the critical estimates and judgements is set out on page 88 and 89.

Adoption of new accounting standards

The following new standards and amendments to accounting standards have been adopted and consistently applied by the Group during the year ended 31 December 2013.

IAS 19 'Employee benefits' (Revised 2011) (IAS 19R) This revised standard requires the elimination of the option for deferred recognition of all changes in the present value of the defined benefit obligation and in the fair value of plan assets (including the corridor approach, which was not applied by the Group). In addition, the amended standard requires a net interest approach, which will replace the expected return on plan assets, and will enhance the disclosure requirements for defined benefit plans. IAS 19R also changes the recognition criteria for termination benefits. Certain termination benefits will now be recognised at a later date unless they form part of a restructuring, as defined in IAS 37. The adoption of this standard has not had a significant financial impact on the Group but has resulted in additional disclosures which are included in note 25.

IFRS 13 'Fair Value Measurement' The standard establishes a single source of guidance under IFRS for all fair value measurements. It does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The application of IFRS 13 has not materially impacted the fair value measurements in the Group's financial statements. The standard also requires some specific additional disclosure on fair values, some of which replace certain existing disclosure requirements in other standards including IFRS 7. The Group provides these disclosures in note 32.

Amendment to IAS 1 'Presentation of financial statements' This amendment requires the grouping of items presented in other comprehensive income (OCI). Items that could be reclassified (or recycled) to profit or loss at a future point in time (e.g., net movement on cash flow hedges and net loss or gain on available for sale financial assets) have to be presented separately from items that will not be reclassified (e.g. remeasurement of the net defined benefit pension liability). The adoption of this amendment has not had a financial impact on the Group but rather has changed the presentation.

Amendment to IFRS 7 'Offsetting Financial Assets and Financial Liabilities' This amendment requires an entity to disclose information about the rights to offset financial instruments and related arrangements. The new disclosures are required both for all recognised financial instruments that are set off in accordance with IAS 32 and for recognised financial instruments that are subject to

Adoption of new accounting standards (continued)

an enforceable master netting arrangement or similar agreement, irrespective of whether the financial instruments are set off in accordance with IAS 32. The adoption of this amendment has had no impact on the financial position of the Group.

Annual Improvements 2009-2011 (the Annual Improvements)
The annual improvements process provides a vehicle for making non-urgent but necessary amendments to IFRSs. These amendments have had no impact on the financial position of the Group.

Details of those IFRS pronouncements which will be relevant to the Group but which were not effective at 31 December 2013 and which have not yet been adopted by the Group are set out on pages 86 and 87.

Comparatives

Additional information has been presented for comparative periods as required in respect of the adoption of new accounting standards during the year. In addition, comparative information has been amended where necessary to ensure consistency with the current period. None of these amendments impact any of the amounts included within the primary statements.

Going concern

The time period that the Directors have considered in evaluating the appropriateness of the going concern basis in preparing the financial statements for the period ended 31 December 2013 is a period of 12 months from the date of approval of these financial statements ('the period of assessment').

In making this assessment the Directors considered the business, capital and funding plans of the Group under base and stress scenarios. The directors also considered the position of the Group's Parent, the Governor and Company of the Bank of Ireland (and Bank of Ireland Group) as, in addition to being the Group's sole shareholder, it is a provider of significant services to the Group under outsourcing arrangements.

Profitability
The Group returned to profitability in 2013, through a combination of efficiently managing its balance sheet and funding costs, improved asset pricing and a significant reduction in loan impairment charges. Reported profits before taxation of £57m represents a year on year improvement of £187 million on 2012, with operating income increasing by £129 million and impairment charges reduced by £58 million.

The Directors are confident that, based on its current plans and forecasts, the Group will remain profitable for the period of assessment.

Capital
The Group has total capital at 31 December 2013 after regulatory deductions of £2.2 billion, a core tier 1 capital ratio of 11.0% and a total capital ratio of 20.3%. The Group has also reviewed the impacts of the Capital Requirements Directive (CRD IV), as part of its capital planning process and based on latest guidance and forecasts the Group continues to anticipate a buffer above minimum regulatory requirements.

The Bank of Ireland Group, the Bank's sole shareholder supported the Bank's acquisition of mortgage assets from its Parent during 2013 through the injection of £35 million of additional capital. The Directors currently do not anticipate the need to further increase the Bank's total capital during the period of assessment.

During the period of assessment the Bank may, in addition to its core activities, purchase further assets from its Parent. Such purchases will only take place if the Bank has sufficient capital and funding and are at the Bank's discretion.

Liquidity and funding
The Bank is self-sufficient from a liquidity perspective, is 100% deposit funded and does not rely on wholesale funding to support core activities, albeit it maintains the operational flexibility to borrow from the market as required.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 72

Going concern (continued)

Customer lending is fully funded by customer deposits and, in line with its liquidity risk appetite, the Group maintains a customer loan to customer deposit ratio of less than 100%. At 31 December 2013 the Group had an actual loan to deposit ratio of 86%. The Bank also maintains a stock of liquid assets in excess of minimum regulatory requirements comprising deposits with the Bank of England; UK government and other sterling denominated securities; and an overnight deposit with the parent company.

In addition the Bank has a Contingency Funding Plan in place detailing options that can be invoked to enable effective management of any liquidity and funding risk. These options include access to contingent liquidity via its holding of £3.5bn of notes issued by Bowbell No 1 plc, a Residential Mortgage Backed Securitisation (RMBS) vehicle and ‘raw loan pools’ that have been confirmed as eligible for pledging to various BOE facilities, including the BOE Discount Window Facility or the Extended Collateral Term Repo (that BOE may open during market stress scenarios).

The Bank’s Parent

The Bank’s Parent is its sole shareholder and provider of capital and is also a major provider of services to the Bank under outsourcing arrangements.

The Directors note that during 2013 there have been on-going developments regarding capital, liquidity and funding and profitability that have further enhanced the position of the Bank’s Parent.

On the basis of the above the Board of the Bank's Parent has concluded that there are no material uncertainties that may cast significant doubt about the Bank of Ireland Group's ability to continue as a going concern and that it is appropriate to prepare accounts on a going concern basis. The audit report on the financial statements of the Bank's Parent is not qualified and does not contain an emphasis of matter paragraph on respect of going concern.

Taking into account the above the Directors of the Bank are satisfied that any risk attaching to the continued ability of the Parent to provide services to the Bank is satisfactorily addressed.

Conclusion

On the basis of the above, the Directors of the Bank consider it appropriate to prepare the financial statements on a going concern basis having concluded that there are no material uncertainties related to events or conditions that may cast significant doubt on the Bank’s ability to continue as a going concern over the period of assessment.

Group financial statements

(1) Subsidiaries

Subsidiaries, which are those companies and other entities (including Special Purpose Entities (SPEs) in which the Group, directly or indirectly, has power to govern the financial and operating policies, generally accompanying a shareholding of more than half of its voting rights, are consolidated.

Assets, liabilities and results of all Group undertakings have been included in the Group financial statements on the basis of financial statements made up to the end of the financial period.

The existence and effect of potential voting rights that are currently exercisable or currently convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. The Group uses the acquisition method of accounting to account for business combinations other than business combination involving entities or businesses under common control. Under the acquisition method of accounting, the consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 73

Group financial statements (continued)

acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets. The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition date fair value of any previous equity interest in the acquiree over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. In addition, foreign exchange gains and losses which arise on the retranslation to functional currency of intercompany monetary assets and liabilities are not eliminated.

Even if there is no shareholder relationship, SPEs are consolidated in accordance with SIC 12, if the Group controls them from an economic perspective. SPEs are consolidated when the substance of the relationship between the Group and that entity indicates control. Potential indicators of control include, amongst others, an assessment of the Group's exposure to the risks and benefits of the SPE. Whenever there is a change in the substance of the relationship between the Group and the SPE, the Group performs a reassessment of consolidation. Indicators for a reassessment of consolidation can include changes in ownership of the SPE, changes in contractual arrangements and changes in the financing structure.

Accounting policies of subsidiaries have been changed, where necessary, to ensure consistency with the policies adopted by the Group.

(2) Associates and Joint Ventures

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

Jointly controlled entities (JCEs) are joint ventures that involve the establishment of a corporation, partnership or other entity in which each venturer has an interest.

Investments in associates and JCEs are accounted for by the equity method of accounting and, except for investments acquired from entities under common control with the Group, are initially recognised at cost. Under the equity method, the Group's share of the post-acquisition profits or losses in associates and joint ventures is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate or joint venture equals or exceeds its interest in the associate or joint venture the Group does not recognise further losses unless it has incurred obligations or made payments on behalf of the associate or joint venture.

Unrealised gains on transactions between the Group and its associates or joint ventures are eliminated to the extent of the Group's interest in the associate / joint venture; unrealised losses are also eliminated on the same basis unless the transaction provides evidence of an impairment of the asset transferred. The Group's investment in associates and joint ventures includes goodwill (net of any accumulated impairment losses) on acquisition.

Jointly controlled operations (JCOs) are joint ventures involving the use of assets and other resources of the venturers rather than the establishment of a separate entity. JCOs are accounted for by recognising the assets controlled by the Group, the liabilities and expenses incurred by the Group, and the Group's share of income earned from the sale of goods or services by the joint venture. Accounting policies of associates and jointly controlled entities have been changed, where necessary, to ensure consistency with the policies adopted by the Group.

(3) Common control transactions

A business combination involving entities or businesses under common control is excluded from the scope of IFRS 3: Business Combinations. The exemption is applicable where the combining entities or businesses are controlled by the same party, both before and after the combination. Where such transactions occur, the Group, in accordance with IAS 8, uses its judgement in developing and applying an accounting policy that is relevant and reliable. In making this judgement, management considers the requirements of IFRS dealing with similar and related issues and the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the framework. Management also considers the most recent pronouncements of other standard setting bodies that use a similar conceptual framework to develop accounting standards, to the extent that these do not conflict with the IFRS Framework or any other IFRS or interpretation.

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

Group financial statements (continued)

Accordingly, the Group applies the guidance set out in FRS 6 Acquisitions and Mergers, as issued by the Accounting Standards Board. Where a transaction meets the definition of a group reconstruction or achieves a similar result, predecessor accounting is applied. The assets and liabilities of the business transferred are measured in the acquiring entity, upon initial recognition, at their existing book value in the consolidated financial statements of the Bank of Ireland Group, as measured under IFRS. The Group incorporates the results of the acquired businesses only from the date on which the business combination occurs.

Similarly, where the Group acquires an investment in an associate or joint venture from an entity under common control with the Group, the investment is recognised initially at its existing book value in the consolidated financial statements of the Bank of Ireland Group.

(4) Non-controlling Interests

Transactions with non-controlling interests where the Group has control over the investee are accounted for using the Economic entity model. This accounting model requires that any surplus or deficit, that arises on any transaction(s) with non-controlling interests to dispose of or to acquire additional interests in the investee, are settled through equity.

(5) Securitisations

Certain Group undertakings have entered into securitisation transactions in order to finance specific loans and advances to customers. All financial assets continue to be held on the Group balance sheet, and a liability recognised for the proceeds of the funding transaction, unless:

- the rights to the cash flows have expired or been transferred;
- substantially all the risks and rewards associated with the financial instruments have been transferred outside the Group, in which case the assets are derecognised in full; or
- a significant portion, but not all, of the risks and rewards have been transferred outside the Group. In this case the asset is derecognised entirely if the transferee has the ability to sell the financial asset. Otherwise the asset continues to be recognised only to the extent of the Group's continuing involvement.

Where the above conditions apply to a fully proportionate share of all or specifically identified cash flows, the relevant accounting treatment is applied to that proportion of the asset.

Foreign currency translation

The Consolidated financial statements of the Group and the financial statements of the Bank are presented in GBP. Foreign currency transactions are translated into functional currency at the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the transaction at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items such as equities, classified as available for sale, are recognised in other comprehensive income.

Interest income and expense

Interest income and expense are recognised in the income statement for all instruments measured at amortised cost using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset, or a financial liability, and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or liability. When calculating the effective interest rate, the Group estimates cash flows, considering all contractual terms of the financial instrument (for example, prepayment options), but does not consider future credit losses. The calculation includes all fees and points, paid or received, between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Interest income and expense (continued)

Once a financial asset, or group of similar financial assets, has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purposes of measuring the impairment loss.

Where the Group revises its estimates of payments or receipts on a financial instrument measured at amortised cost, the carrying amount of the financial instrument (or group of financial instruments) is adjusted to reflect actual and revised estimated cash flows. The Group recalculates the carrying amount by computing the present value of estimated future cash flows at the financial instrument's original effective interest rate. The adjustment is recognised in profit or loss as income or expense.

Fee and commission income and expense

Fees and commissions which are not an integral part of the effective interest rate of a financial instrument are generally recognised as the related services are provided. Service fee income arising from other money transmission services, including ATM and credit cards, is accrued once the transactions take place. Similarly, fees and commissions due to third parties in relation to credit card, ATM, and other banking services, including sales commissions, are accrued over the period the service is provided.

Commissions and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as the acquisition of loans, shares or other securities or the purchase or sale of businesses, are recognised on completion of the underlying transaction. Loan commitment fees for loans that are likely to be drawn down, are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan once drawn

Operating profit / loss

Operating profit / loss includes the Group's earnings from ongoing activities after impairment charges and before share of profit or loss on jointly controlled entities (after tax).

Leases

Lessor
When assets are held under a finance lease, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is included within net interest income and is recognised over the term of the lease reflecting a constant periodic rate of return on the net investment in the lease.

Financial assets

(1) Classification, Recognition and Measurement
The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables; and available for sale financial assets. The Group determines the classification of its financial assets at initial recognition.

Regular way purchases and sales of financial assets are recognised on the trade date, which is the date the Group commits to purchase or sell the asset.

(a) Financial assets at fair value through profit or loss
Financial assets at fair value through profit or loss can either be held for trading, if acquired principally for the purpose of selling in the short term, or designated at fair value through profit or loss at inception.

Financial assets (continued)

A financial asset may be designated at fair value through profit or loss only when:

(i) it eliminates, or significantly reduces, a measurement or recognition inconsistency (an accounting mismatch), that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on a different basis;

(ii) a group of financial assets, financial liabilities, or both, is managed and its performance is evaluated on a fair value basis, in accordance with documented risk management or investment strategy; or

(iii) a contract contains one or more embedded derivatives that significantly changes the cash flows of the contract and the separation of the embedded derivative(s) is not prohibited.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods, or services directly to a debtor with no intention of trading the receivable. Loans are recorded at fair value plus transaction costs on initial recognition. They are subsequently accounted for at amortised cost, using the effective interest method.

Where the Group acquires a portfolio of financial assets from an entity under common control with the Group, in a transaction which is not a business combination, the financial assets are measured on initial recognition at their fair value plus transaction costs.

To establish fair value, the Group uses a valuation technique, which reasonably reflects how the market could be expected to price the assets, and whose variables include market data. This valuation technique incorporates both expected credit losses and the differential between the contractual interest rates on the assets and current market interest rates for similar assets.

The difference between the initial carrying value of the assets and their principal balances is considered to be a ‘fair value adjustment’. The portion of this fair value adjustment which relates to interest rate differentials is amortised to the income statement, as part of the effective interest rate of the assets, over their remaining lives.

The portion of the fair value adjustment which relates to expected credit losses is subsequently reduced by actual write offs of loans during each period. Additionally, an annual review is performed to ensure that the remaining amount of this portion of the fair value adjustment is adequate to cover future expected losses on the assets. This review identifies either the amount of any impairment provision required to be immediately recognised, if the remaining adjustment is less than the incurred losses on the assets, or any surplus amount of fair value adjustment which must be released to the income statement if it is no longer required to cover future expected losses.

(c) Available for sale

Available for sale financial assets are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates.

Purchases and sales of available for sale financial assets are recognised on trade date. They are initially recognised at fair value plus transaction costs. Fair value movements are recognised in other comprehensive income. Interest is calculated using the effective interest method and is recognised in the income statement.

If an available for sale financial asset is derecognised or impaired, the cumulative gain or loss previously recognised in other comprehensive income is reclassified to the income statement.

Dividends on available for sale equity instruments are recognised in the income statement when the Group’s right to receive payment is established.

(2) Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 77

Financial liabilities

The Group has two categories of financial liabilities: those that are carried at amortised cost and those that are carried at fair value through profit or loss. Financial liabilities are initially recognised at fair value (normally the issue proceeds i.e. the fair value of consideration received) less, in the case of financial liabilities subsequently carried at amortised cost, transaction costs. For liabilities carried at amortised cost, any difference between the proceeds, net of transaction costs, and the redemption value is recognised in the income statement using the effective interest method.

A liability may be designated as fair value through profit or loss only when:

(i) it eliminates, or significantly reduces, a measurement or recognition inconsistency ('an accounting mismatch'), that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on a different basis;

(ii) a group of financial assets, financial liabilities, or both, is managed and its performance is evaluated on a fair value basis in accordance with documented risk management or investment strategy; or

(iii) a contract contains one or more embedded derivatives that significantly changes the cash flows of the contract and the separation of the embedded derivative(s) is not prohibited.

The Group designates certain financial liabilities at fair value through profit or loss, as set out in note 31 to the consolidated financial statements and note 'v' to the Bank financial statements.

Financial liabilities are derecognised when they are extinguished, that is, when the obligation is discharged, cancelled or expires.

Valuation of financial instruments

The Group recognises assets and liabilities designated at fair value through profit or loss, derivatives and available-for-sale financial assets at fair value in the balance sheet. 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 in the principal, or in its absence, the most advantageous market to which the Group has access at that date.

The fair values of financial assets and liabilities traded in active markets are based on unadjusted bid and offer prices respectively. If an active market does not exist, the Group establishes fair value using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. To the extent possible, these valuation techniques use observable market data. Where observable data does not exist, the Group used estimates based on the best information available.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, in an arm's length transaction, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique which uses only observable market inputs. When such evidence exists, the initial valuation of the instrument may result in the Group recognising a profit on initial recognition. In the absence of such evidence, the instrument is initially valued at the transaction price. Any day one profit is deferred and recognised in the income statement to the extent that it arises from a change in a factor that market participants would consider in setting a price. Straight line amortisation is used where it approximates to the amount. Subsequent changes in fair value are recognised immediately in the income statement without the reversal of deferred day one profits or losses. Where a transaction price in an arm's length transaction is not available, the fair value of the instrument at initial recognition is measured using a valuation technique.

For liabilities designated at fair value through profit or loss, the fair values reflect changes in the Group's own credit spread.

The fair values of the Group's financial assets and liabilities are disclosed within note 32, together with a description of the valuation technique used for each asset or liability category. For assets or liabilities recognised at fair value on the balance sheet, a description is given of any inputs into valuation models that have the potential to significantly impact the fair value, together with an estimate of the impact of using reasonably possible alternative assumptions.

The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change occurred.

Sale and repurchase agreements

Assets sold subject to repurchase agreements (repos) are retained on the balance sheet and reclassified as pledged assets when the transferee has the right by contract or custom to sell or re-pledge the collateral; the counterparty liability is included in deposits by banks or customer accounts, as appropriate.

Securities purchased under agreements to resell (reverse repos) are treated as collateralised loans and recorded as loans and advances to banks or customers, as appropriate. The difference between sale and repurchase price is treated as interest and recognised in the income statement over the life of the agreement using the effective interest method. Securities lent to counterparties are also retained on the balance sheet.

Securities borrowed are not recognised in the financial statements, unless these are sold to third parties, in which case the purchase and sale are recorded with the gain or loss included in trading income. The obligation to return the securities is recorded at fair value as a trading liability.

Derivative financial instruments and hedge accounting

Derivatives are initially recognised at fair value on the date on which the contract is entered into and are subsequently remeasured at their fair value at each balance sheet date. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Fair value gains or losses on derivatives are normally recognised in the income statement. However where they are designated as hedging instruments, the treatment of the fair value gains and losses depends on the nature of the hedging relationship.

The Group designates certain derivatives as either:

(i) hedges of the exposure to changes in the fair value of recognised assets or liabilities that is attributable to a particular risk (fair value hedge); or

(ii) hedges of future cash flows attributable to a recognised asset or liability, or a highly probable forecast transaction (cash flow hedge).

Hedge accounting is applied to these derivatives provided certain criteria are met. The Group documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

(a) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If the criteria for hedge accounting cease to be met, no further adjustments are made to the hedged item for fair value changes attributable to the hedged risk. The cumulative adjustment to the carrying amount of a hedged item is amortised to profit or loss over the period to maturity of the hedged item using the effective interest method.

(b) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in the income statement. Amounts accumulated in other comprehensive income are reclassified to the income statement in the periods in which the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in other comprehensive income at that time remains in other comprehensive income and is recognised in the income statement when the forecast transaction occurs. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in other comprehensive income is immediately reclassified to the income statement.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 79

Impairment of financial assets

(a) Assets carried at amortised cost

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset, or group of financial assets, is impaired. A financial asset, or a group of financial assets, is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that a financial asset, or group of assets, is impaired includes observable data that comes to the attention of the Group about the following loss events:

(i) delinquency in contractual payments of principal or interest;
(ii) cash flow difficulties;
(iii) breach of loan covenants or conditions;
(iv) deterioration of the borrower's competitive position;
(v) deterioration in the value of collateral;
(vi) external rating downgrade below an acceptable level; and
(vii) initiation of bankruptcy proceedings.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss, is or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and advances carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred), discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Group's grading process that considers asset type, industry, geographical location, collateral type, past due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the Group and historical loss experience for assets with credit risk characteristics similar to those in the Group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

Impairment of financial assets (continued)

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the charge for loan impairment in the income statement.

Forbearance

Forbearance occurs when a borrower is granted a temporary or permanent concession or agreed change to a financial asset ('forbearance measure') for reasons relating to the actual or apparent financial stress or distress of that borrower. If the concession or agreed change to a financial asset granted to a borrower is not related to the actual or apparent financial stress or distress of that borrower, forbearance has not occurred.

The Group performs an assessment of a customer's financial circumstances and ability to repay prior to any decision to grant forbearance. This assessment includes an individual assessment for impairment of the financial asset. If the Group determines that no objective evidence of impairment exists for an individually assessed forborne asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment.

Where the forborne financial asset is considered to be impaired the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the asset's original effective interest rate before the modification of terms. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a forborne asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract before the modification of terms. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

Where a forborne financial asset in the non-mortgage book is subject to forbearance and no specific provision is required, the asset is reported as forborne and is not reported as impaired. However, where a specific provision is required the asset is reported as impaired and is not reported as forborne. For residential mortgages, exposures that are subject to forbearance and have a specific provision are reported as both forborne and impaired.

Assets to which forbearance has been applied continue to be reported as forborne until the forbearance measure expires or the asset is repaid.

Where the cash flows from a forborne financial asset are considered to have expired, the original asset is derecognised and a new asset is recognised, initially measured at fair value. Circumstances where the cash flows from a forborne financial asset may be considered to have expired include where the terms of the new asset differ substantially from those of the original asset either qualitatively or quantitatively. Any difference between the carrying value of the original asset and the fair value of the new asset on initial recognition are recognised in the income statement. Interest accrues on the new asset based on the current market rates in place at the time of the renegotiation.

Non-forbearance renegotiation

Where a concession or agreed change to a financial asset is not directly linked to apparent financial stress or distress, these amendments are not considered forbearance. The changes in expected cash flows are accounted for under IAS 39.AG8 i.e. the carrying amount of the asset is adjusted to reflect the revised estimated cash flows discounted at the original effective interest rate, before the modification of terms. If a renegotiated asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. Any difference between the asset's carrying amount and the present value of estimated future cash flows is reflected in the income statement. However, where cash flows on the original asset have considered to have expired, the original asset is derecognised and a new asset is recognised at fair value. Any difference arising between the derecognised asset and the new asset is recognised in the income statement. The Risk management section on page 46 contains further details on loan loss provisioning methodology.

(b) Available for sale financial assets

The Group assesses, at each balance sheet date, whether there is objective evidence that an available for sale financial asset is impaired. In addition to the factors set out above, a significant or prolonged decline in the fair value of an investment in an available for sale equity instrument below its cost is considered in determining whether an impairment loss has been incurred. If an impairment loss has been incurred, the cumulative loss that had been recognised in other comprehensive income is removed from equity and

Impairment of financial assets (continued)

recognised in the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed through the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

Property, plant and equipment

Freehold land and buildings are initially recognised at cost, and subsequently are revalued annually to open market value by independent external valuers. Revaluations are made with sufficient regularity to ensure that the carrying amount does not differ materially from the open market value at the balance sheet date.

All other property, plant and equipment, including freehold and leasehold adaptations, are stated at historical cost less accumulated depreciation. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Increases in the carrying amount arising on the revaluation of land and buildings are recognised in other comprehensive income. Decreases that offset previous increases on the same asset are recognised in other comprehensive income: all other decreases are charged to the income statement.

The Directors consider that residual values of freehold and long leasehold property based on prices prevailing at the time of acquisition or subsequent valuation are such that depreciation is not material.

Depreciation is calculated on the straight line method to write down the carrying value of other items of property, plant and equipment to their residual values over their estimated useful lives as follows:

- Adaptation works on freehold and leasehold property - Fifteen years, or the remaining period of the lease; and
- Computer and other equipment - Maximum of ten years.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. Property, plant and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if its carrying amount is greater than its estimated recoverable amount. The estimated recoverable amount is the higher of the asset's fair value less costs to sell or its value in use.

Gains and losses on the disposal of property, plant and equipment are determined by reference to their carrying amount and are taken into account in determining profit before tax. If the asset being disposed of had previously been revalued then any amount in other comprehensive income relating to that asset is reclassified to retained earnings on disposal, rather than the income statement.

Intangible assets

(a) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives, which is normally between five and ten years.

Costs associated with developing or maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the Group and which will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include software development, employee costs and an appropriate portion of relevant overheads. Computer software development costs recognised as assets are amortised using the straight line method over their useful lives, which is normally between five and ten years.

Intangible assets (continued)

Computer software is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if its carrying amount is greater than its estimated recoverable amount. The estimated recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

(b) Other intangible assets

Other intangible assets are carried at cost less amortisation and impairment, if any, and are amortised on a straight line basis over their useful lives which range from five years to twenty years and reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if its carrying amount is greater than its estimated recoverable amount. The estimated recoverable amount is the higher of the asset's fair value less costs to sell or its value in use.

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Provision is made for the anticipated costs of restructuring, including related redundancy costs, when an obligation exists. An obligation exists when the Group has a detailed formal plan for restructuring a business and has raised valid expectations in those affected by the restructuring by starting to implement the plan or announcing its main features.

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised but are disclosed unless the probability of their occurrence is remote.

Employee benefits

(a) Pension obligations

The Group operates two pension schemes; Life balance 2 and the NIIB defined benefit scheme. The schemes are funded and the assets of the schemes are held in separate trustee administered funds. A defined benefit plan is a pension plan that defines an amount of pension benefit to be provided, usually as a function of one or more factors such as age, years of service or compensation.

The asset or liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date minus the fair value of plan assets. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates on high quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability

Service cost is recognised in profit or loss within operating expenses, together with net interest on the net defined benefit liability / (asset).

Remeasurements of the net defined benefit liability / (asset), including:

- actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions; and
- the return on plan assets, excluding amounts included in net interest on the net defined benefit liability / (asset);

are recognised in other comprehensive income.

Past service cost is the change in the present value of the defined benefit obligation resulting from a plan amendment or curtailment, and is recognised as an expense at the earlier of:

- when the plan amendment or curtailment occurs; and
- when the Group recognises related restructuring costs or termination benefits.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 83

Employee benefits (continued)

Past service cost is recognised within operating expenses unless it meets the criteria for separate presentation under IAS 1.

A plan amendment occurs when the Group introduces, or withdraws, a defined benefit plan, or changes the benefits payable under an existing plan. A curtailment occurs when the Group significantly reduces the number of employees covered by a plan. Past service cost may be either positive or negative.

(b) Short term employee benefits

Short term employee benefits, such as salaries and other benefits, are accounted for on an accruals basis over the period in which the employees' service is rendered. Bonuses are recognised where the Group has a legal or constructive obligation to employees that can be reliably measured.

(c) Termination payments

Termination payments are recognised as an expense at the earlier of:

- When the Group can no longer withdraw the offer of those benefits; and
- When the Group recognises costs for a restructuring that is within the scope of IAS 37 and involves the payment of termination benefits.

For this purpose, in relation to termination benefits for voluntary redundancies, the Group is considered to be no longer able to withdraw the offer on the earlier of the following dates:

- when the employee accepts the offer; and
- when a restriction (e.g. a legal, regulatory or contractual requirement) on the Group's ability to withdraw the offer takes effect.

Termination benefits are recognised within operating expenses unless they meet the criteria for separate presentation, as set out in IAS 1. The Group measures termination benefits on initial recognition and measures and recognises subsequent changes in accordance with the nature of the benefit.

Income taxes

(a) Current income tax

Income tax payable on profits is recognised as an expense in the year in which profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available, against which these losses can be utilised.

(b) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and tax laws) that have been enacted, or substantively enacted, by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The rates enacted, or substantively enacted, at the balance sheet date, are used to determine deferred income tax. However, the deferred income tax is not accounted for if it arises 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 assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised and by reference to the expiry dates (if any) of the relevant unused tax losses or tax credits. Deferred tax assets and liabilities are not discounted.

Deferred income tax is provided on temporary differences arising from investments in subsidiaries, associates and jointly controlled entities, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the difference will not reverse in the foreseeable future.

Deferred tax on items taken to other comprehensive income is also recognised in other comprehensive income and is subsequently reclassified to the income statement, together with the deferred gain or loss.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise cash in hand and balances with Central Banks and other banks, which can be withdrawn on demand. It also comprises balances with an original maturity of less than three months.

Share capital and reserves

(1) Stock issue costs
Incremental external costs, directly attributable to the issue of new equity shares or options, are shown in equity as a deduction, net of tax, from the proceeds.

(2) Dividends on ordinary shares
Dividends on ordinary shares are recognised in equity in the year in which they are approved by the Bank's shareholders or the Board of Directors, as appropriate.

(3) Available for sale reserve
The available for sale reserve represents the cumulative change in fair value of available for sale financial assets.

(4) Cash flow hedge reserve
The cash flow hedge reserve represents the cumulative changes in fair value excluding any ineffectiveness of cash flow hedging derivatives. These are transferred to the income statement when the hedged transactions impact the Group's profit or loss.

(5) Capital Contribution
The capital contribution is measured as the initial amount of cash or other assets received.

Where a financial instrument is issued by the Group to a party, acting in its capacity as a stockholder, other than at arm's length, which results in an increase of the net assets of the Group, the difference between the fair value of the transaction and the transaction price is considered to be a capital contribution from the stockholder and is credited to this reserve.

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right of set off and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Collateral

The Group enters into master netting agreements with counterparties, to ensure that if an event of default occurs, all amounts outstanding with those counterparties will be settled on a net basis.

The Group obtains collateral in respect of customer liabilities where this is considered appropriate. The collateral normally takes the form of a lien over the customer's assets and gives the Group a claim on these assets for both existing and future liabilities. The collateral is, in general, not recorded on the Group's balance sheet.

The Group also receives collateral in the form of cash or securities in respect of other credit instruments, such as stock borrowing contracts and derivative contracts, in order to reduce credit risk. Collateral received in the form of cash is recorded on the balance sheet, with a corresponding liability recognised within deposits from banks or deposits from customers. Any interest payable arising is recorded as interest expense.

In certain circumstances, the Group pledges collateral in respect of liabilities or borrowings. Collateral pledged, in the form of securities or loans and advances, continues to be recorded on the balance sheet. Collateral placed in the form of cash is recorded in loans and advances to banks or customers. Any interest receivable arising is recorded as interest income.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 85

Financial guarantees

Financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities ('facility guarantees'), and to other parties in connection with the performance of customers under obligations related to contracts, advance payments made by other parties, tenders, retentions, and the payment of import duties. Financial guarantees are initially recognised in the financial statements at fair value on the date that the guarantee is given. Subsequent to initial recognition, the Group's liabilities under such guarantees are measured at the higher of the initial measurement, less amortisation calculated to recognise in the income statement the fee income earned over the year, and the best estimate of the expenditure required to settle any financial obligation arising as a result of the guarantees at the balance sheet date.

Any increase in the liability relating to guarantees is taken to the income statement and recognised on the balance sheet within provisions for undrawn contractually committed facilities and guarantees.

Operating segments

The segmental analysis of the Group's results and financial position is set out in note 1. The Group has identified four reportable operating segments, which are as follows: Great Britain Consumer Banking, Northern Ireland, Great Britain Business Banking and Other.

These segments have been identified on the basis that the chief operating decision-maker uses information based on these segments to make decisions about assessing performance and allocating resources. The analysis of results by operating segment is based on management accounts information.

Transactions between the operating segments are on normal commercial terms and conditions. Internal charges and transfer pricing adjustments have been reflected in the performance of each segment. Revenue sharing agreements are used to allocate external customer revenues to operating segments on a reasonable basis.

Materiality

In its assessment of materiality, the Group considers the impact of any misstatements based on both:
- the amount of the misstatement originating in the current year income statement; and
- the effects of correcting the misstatement existing in the balance sheet at the end of the current year irrespective of the year in which the misstatement occurred.

Impact of new accounting standards

The following standards, interpretations and amendments to standards will be relevant to the Group but were not effective at 31 December 2013 and have not been applied in preparing these financial statements. The Group's initial view of the impact of these accounting changes is outlined below.

Pronouncement	Nature of change	Effective date	Impact
Amendments to IAS 32 'Financial Instruments' on Asset and Liability Offsetting	These amendments are to the application guidance in IAS 32, 'Financial Instruments: Presentation', that clarify some of the requirement for offsetting financial assets and financial liabilities on the balance sheet. Some gross settlement systems may qualify for offsetting where they exhibit certain characteristics akin to net settlement.	IAS 32: Financial periods starting on or after 1 January 2014.	Additional disclosures will be presented at 31 December 2014 in line with requirements.
IFRS 10 'Consolidated Financial Statements'	This standard replaces IAS 27, 'Consolidated and Separate Financial Statements' and SIC-12, 'Consolidation – Special Purpose Entities'. It establishes a single control model that applies to all entities, including those that were previously considered special purpose entities under SIC-12. An investor controls an investee when it is exposed to, or has rights to, variable returns from the investee, and has the ability to affect those returns through its power over the investee. The assessment of control is based on all facts and circumstances, and the conclusion is reassessed if there is an indication that there are changes in facts and circumstances. The new standard was endorsed by the EU on 11 December 2012.	Financial periods beginning on or after 1 January 2014 for entities that apply IFRS as adopted for use in the EU.	No change to Group structure.
IFRS 11 'Joint arrangements'	IFRS 11 supersedes IAS 31, 'Interests in Joint Ventures' and SIC-13, 'Jointly-controlled Entities – Non monetary Contributions by Venturers'. IFRS 11 classifies joint arrangements as either joint operations or joint ventures and focuses on the nature of the rights and obligations of the arrangement. IFRS 11 requires the use of the equity method of accounting for joint arrangements by eliminating the option to use the proportionate consolidation method, which is not applied by the Group. The new standard was endorsed by the EU on 11 December 2012.	Accounting periods starting on or after 1 January 2014 for entities that apply IFRS as adopted for use in the EU.	Not significant
IFRS 12 'Disclosures of Interests in Other Entities'	IFRS 12 establishes the provision of information on the nature, associated risks, and financial effects of interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities, as disclosure objectives. IFRS 12 requires more comprehensive disclosure, and specifies minimum disclosures that an entity must provide to meet the disclosure objectives. While each of the standards is effective for annual periods beginning on or after 1 January 2014 (for entities that apply IFRS as adopted for use in the EU), with earlier application permitted as long as each of the other standards is also early applied, entities are permitted to include any of the disclosure requirements in IFRS 12 into their consolidated financial statements without early adopting IFRS 12. The new standard was endorsed by the EU on 11 December 2012.	Accounting periods starting on or after 1 January 2014 for entities that apply IFRS as adopted for use in the EU.	No financial impact Additional disclosures will be presented at 31 December 2014 in line with requirements.

Impact of new accounting standards (continued)

Pronouncement	Nature of change	Effective date	Impact
IAS 27 (revised). 'Separate Financial Statements'	IAS 27 (revised) includes the provisions on separate financial statements that are left after the control provisions of IAS 27 have been included in the new IFRS 10. The revised standard was endorsed by the EU on 11 December 2012.	Accounting periods starting on or after 1 January 2014 for entities that apply IFRS as adopted for use in the EU.	Not significant
IAS 28 (revised). 'Investments in Associates and Joint Ventures'	IAS 28 (revised) includes the requirements for joint ventures, as well as associates to be equity accounted following the issue of IFRS 11. The revised standard was endorsed by the EU on 11 December 2012.	Accounting periods starting on or after 1 January 2014 for entities that apply IFRS as adopted for use in the EU.	Not significant
IFRIC Interpretation 21: Levies	This Interpretation deals with accounting for levies imposed by governments, principally when an entity should recognise a liability to pay a levy. The Interpretation clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. The new interpretation is still subject to EU endorsement.	Financial periods beginning on or after 1 January 2014.	Not significant
IFRS 9 'Financial instruments'	IFRS 9 is the first step in the process to replace IAS 39, 'Financial instruments: recognition and measurement'. The first stage of IFRS 9 dealt with the classification and measurement of financial assets and was issued in November 2009. An addition to IFRS 9, dealing with financial liabilities, was issued in October 2010. In November 2013, further guidance was given on hedging and own credit risk for financial liabilities at fair value. The main changes from IAS 39 are summarised as follows: • The multiple classification model for financial assets in IAS 39 is replaced with a single model that has only two classification categories: amortised cost and fair value; • Classification under IFRS 9 is driven by the entity's business model for managing financial assets and the contractual characteristics of the financial assets; • The requirement to separate embedded derivatives from financial asset hosts is removed; • The cost exemption for unquoted equities is removed; • Most of IAS 39's requirements for financial liabilities are retained, including amortised cost accounting, for most financial liabilities; • Guidance on separation of embedded derivatives will continue to apply to host contracts that are financial liabilities; and • Fair value changes attributable to changes in own credit risk for financial liabilities designated under the fair value option, other than loan commitments and financial guarantee contracts, are required to be presented in the Statement of Other Comprehensive Income, unless the treatment would create or enlarge an accounting mismatch in profit or loss. These amounts are not subsequently reclassified to the income statement but may be transferred within equity. This change can now be early adopted; and • new general hedge accounting model. The new standard is still subject to EU endorsement.	The mandatory effective date of 1 January 2015 has been removed pending further developments of the standard.	The Group is assessing the impacts of adopting IFRS 9. The impact of IFRS 9 is expected to change as a consequence of further developments resulting from the IASB's financial instruments project.

Critical accounting estimates and judgements

In preparing the financial statements, the Group makes estimates and judgements that affect the reported amounts of assets, liabilities, revenues, and expenses. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. As management judgement involves an estimate of the likelihood of future events, actual results could differ from those estimates, which could affect the future reported amounts of assets and liabilities. The estimates and judgements that have had the most significant effect on the amounts recognised in the Group's financial statements are set out below.

(a) Impairment charges on financial assets
The Group reviews its loan portfolios for impairment on an ongoing basis. The Group first assesses whether objective evidence of impairment exists, both individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. Impairment provisions are also recognised for losses not specifically identified but which, experience and observable data indicate, are present in the portfolio at the date of assessment.

Management uses estimates, based on historical loss experience for assets with credit risk characteristics, and objective evidence of impairment, similar to those in the portfolio, when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. The use of historical loss experience is supplemented with management judgment to assess whether current economic and credit conditions are such that the actual level of inherent losses is likely to differ from that suggested by historical experience. In normal circumstances, historical experience provides objective and relevant information from which to assess inherent loss within each portfolio. In other circumstances, historical loss experience provides less relevant information about the inherent loss in a given portfolio at the balance sheet date; for example, where there have been changes in economic conditions, such that the most recent trends in risk factors are not fully reflected in the historical information. In these circumstances, such risk factors are taken into account when calculating the appropriate levels of impairment allowances, by adjusting the impairment loss derived solely from historical loss experience.

The detailed methodologies, areas of estimation, and judgement, applied in the calculation of the Group's impairment charge on financial assets, are set out in the Risk management section on pages 46 to 48.

The estimation of impairment losses is subject to uncertainty, which increased in the recent economic environment, and is sensitive to factors such as the level of economic activity, unemployment rates, bankruptcy trends, property price trends, and interest rates. The assumptions underlying this judgement are subjective. The methodology and the assumptions used in calculating impairment losses are reviewed regularly, in light of differences between loss estimates and actual loss experience. See note 17 for more information.

(b) Taxation
The taxation charge accounts for amounts due to UK authorities, and includes estimates based on a judgement of the application of law and practice, in certain cases, to determine the quantification of any liabilities arising. In arriving at such estimates, management assesses the relative merits and risks of tax treatments assumed, taking into account statutory, judicial, and regulatory guidance and, where appropriate, external advice.

At 31 December 2013, the Group had a net deferred tax asset of £128 million (31 December 2012: £74 million), of which £117 million (31 December 2012: £66 million) related to incurred trading losses. See note 26.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available, against which deductible temporary differences and unutilised tax losses can be utilised. The recognition of a deferred tax asset relies on management's judgements surrounding the probability and sufficiency of future taxable profits, and the future reversals of existing taxable temporary differences.

To the extent that the recognition of a deferred tax asset is dependent on sufficient future profitability, a degree of estimation and the use of assumptions are required. The Group's judgement takes into consideration the impact of both positive and negative evidence, including historical financial performance, projections of future taxable income, the impact of tax legislation, and future reversals of existing taxable temporary differences.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 89

Critical accounting estimates and judgements (continued)

The most significant judgement relates to the Group's assessment of the recoverability of the portion of the deferred tax asset relating to trading losses. Under current UK tax legislation; there is no time restriction on the utilisation of these losses.

Based on its projection of future taxable income, the Group has concluded that it is probable that sufficient taxable profits will be generated to recover this deferred asset and it has been recognised in full.

As set out in note 26, during the year the Group reassessed the value of losses acquired from its Parent on the transfer of business assets in 2010, and consequently has recognised a deferred tax asset of £86 million in respect of the taxation benefit of losses transferred from the Parent.

The amount recognised represents the Group's best estimate of the taxation benefit of these losses. There is a possibility that the ultimate outcome could be different from the amounts that are currently recorded and any such differences will impact the deferred tax assets in the period in which such outcome is determined.

(c) Unwind of fair value adjustments on acquired mortgages

During 2012 and 2013 the Group acquired a number of tranches of mortgages from the Parent at fair value. These assets are initially recognised on the balance sheet at fair value plus transaction costs. The differential between the initial carrying value of the assets and the principal balances is considered to be a 'fair value adjustment'. The portion of this fair value adjustment which relates to interest rate differentials is amortised to the income statement, as part of the effective interest rate of the assets, over their remaining lives. The portion of the fair value adjustment also includes an element relating to the present value of expected losses, and the discount on this element also unwinds through the income statement over their remaining lives.

The timing of the unwind of the fair value adjustment requires significant management judgement, which impacts on the amount of interest income recognised in the year. In 2013, there was a benefit of £45 million (2012: £9 million) to the income statement from the unwind of the fair value adjustment being credited to the income statement.

Notes to the Consolidated Financial Statements

Index

		Page
1.	Operating segments	91
2.	Interest income	93
3.	Interest expense	93
4.	Fee and commission income and expense	94
5.	Net trading income	94
6.	Other operating income	95
7.	Operating expenses	95
8.	Auditors' remuneration	96
9.	Impairment charges on financial assets	96
10.	Share of profit after tax of jointly controlled entity	96
11.	Taxation	97
12.	Cash and cash equivalents	98
13.	Derivative financial instruments	98
14.	Loans and advances to banks	100
15.	Available for sale financial assets	101
16.	Loans and advances to customers	101
17.	Impairment provisions	103
18.	Interest in jointly controlled entity	104
19.	Intangible assets	105
20.	Other assets	106
21.	Deposits from banks	106
22.	Customer accounts	106
23.	Other liabilities	107
24.	Provisions	107
25.	Retirement benefit obligations	108
26.	Deferred tax	114
27.	Subordinated liabilities	115
28.	Contingent liabilities and commitments	116
29.	Share capital	117
30.	Liquidity risk	118
31.	Measurement basis of financial assets and financial liabilities	119
32.	Fair value of financial assets and financial liabilities	121
33.	Related party transactions	125
34.	Offsetting financial assets and liabilities	129
35.	Principal undertakings	130
36.	Other subsidiaries	130
37.	Common control transactions	131
38.	Post balance sheet events	132
39.	Approval of financial statements	132

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:33 Page 91

1 Operating segments

The Group has four reportable operating segments which reflect the internal financial and management reporting structure and are organised as follows:

Great Britain (GB) Consumer Banking
The business offers a wide range of products under the Bank of Ireland, Post Office, Bristol & West and NIIB brands. The Post Office product proposition includes deposits, ATM's, mortgages, personal loans, credit and travel cards, insurance and foreign exchange through the Group's joint venture operation under FRESH. The Group's investment in FRESH at 31 December 2013 was £55 million.

Northern Ireland (NI)
The business includes the results of the Northern Ireland Bank of Ireland branded branch network and business centres, together with the credit card and mortgage portfolio and the note issuing activity in Northern Ireland.

Great Britain (GB) Business Banking
The business includes commercial lending and retail deposits. As a result of the Parent's EU restructuring requirements and following agreement with the EU Commission during 2013, the strategy for the business is now a managed deleverage of the loan book over the medium term.

Other
This comprises the associated costs of management of the Group's funding, liquidity and capital position, together with the cost of central risk and control functions and regulatory costs including the Financial Services Compensation Scheme (FSCS) levy.

Basis of preparation of segmental information
The analysis of results by operating segment is based on the information used by management to allocate resources and assess performance. Transactions between the business segments are on normal commercial terms and conditions. Internal charges and transfer pricing arrangements have been reflected in the performance of each business. The chief operating decision maker relies primarily on income reported on a net basis and the measures of segmental assets and liabilities provided are not adjusted for revenue sharing agreements. As a result of this segmental interest income is reported in the financial statements net of interest expense. The Group's management reporting and controlling systems use accounting policies that are the same as those referenced in 'Group Accounting Policies' on pages 70 to 89. The Group measures the performance of its operating segments through a measure of segmental profit or loss in its internal management reporting systems.

Geographical areas
The Group has no material operations outside the UK and therefore no secondary geographical area information is presented.

Gross revenue comprises interest income, fee and commission income, net trading income, other operating income, and share of results of jointly controlled entities. There were no revenues deriving from transactions with a single external customer that amounted to 10% or more of the Group's revenues.

1 Operating segments (continued)

Year ended 31 December 2013	**GB Consumer banking £m**	**NI £m**	**GB Business banking £m**	**Other £m**	**Inter-segment elimination £m**	**Total £m**
Net interest income	313	83	33	(14)	-	415
Other income	(23)	27	4	(1)	-	7
Total operating income	290	110	37	(15)	-	422
Amortisation of intangibles	(4)	-	-	(3)	-	(7)
Other operating expenses	(117)	(85)	(26)	(39)	-	(267)
Operating profit / (loss) before impairment charges on financial assets	169	25	11	(57)	-	148
Impairment charges on financial assets	(18)	(75)	(32)	-	-	(125)
Share of profit after tax of jointly controlled entities	34	-	-	-	-	34
Profit / (loss) before taxation	185	(50)	(21)	(57)	-	57

Year ended 31 December 2012	GB Consumer banking £m	NI £m	GB Business banking £m	Other £m	Inter-segment elimination £m	Total £m
Net interest income	185	75	39	(36)	-	263
Other income	(2)	28	5	(1)	-	30
Total operating income	183	103	44	(37)	-	293
Amortisation of intangibles	(8)	-	-	-	-	(8)
Other operating expenses	(101)	(91)	(30)	(42)	-	(264)
Operating profit / (loss) before impairment charges on financial assets	74	12	14	(79)	-	21
Impairment charges on financial assets	(29)	(124)	(30)	-	-	(183)
Share of profit after tax of jointly controlled entities	32	-	-	-	-	32
Profit / (loss) before taxation	77	(112)	(16)	(79)	-	(130)

2 Interest income

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Loans and advances to customers	715	616
Cash and balances with Central Banks	25	29
Available for sale financial assets	4	2
Loans and advances to banks	315	618
Finance leases and hire purchase receivables	42	40
Interest income	**1,101**	**1,305**

Included in interest income for the year ended 31 December 2013 is £315 million in respect of income earned by the Group on loans and advances to banks in respect of amounts placed with the Parent (year ended 31 December 2012: £616 million).

Interest income received from the Parent and interest paid to the Parent in 2012 included amounts arising from the Parent applying a standard transfer pricing methodology for all businesses in respect of deposits placed with, or amounts borrowed from the Parent. In 2013 the Group started to move away from the aforementioned legacy transfer pricing method due to the development of its own internal transfer pricing process. This has resulted in a net transfer pricing income from the Parent being allocated to the Group in 2013, rather than a gross transfer pricing income in respect of amounts placed with the Parent and a gross transfer pricing expense in respect of amounts borrowed from the Parent. This is the primary driver of the reduction of £303 million in interest income on loans and advances to banks and the reduction of £249 million in interest expense on deposits from banks.

Also included in interest income for year ended 31 December 2013 is £24 million in respect of interest arising on financial assets, on which an impairment provision has been recognised (year ended 31 December 2012: £27 million).

Finance lease and hire purchases receivables interest income arises from NIIB Group Ltd.

3 Interest expense

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Customer accounts	424	538
Deposits from banks	210	459
Subordinated liabilities	52	45
Interest expense	**686**	**1,042**

Included in interest expense for the year ended 31 December 2013 is £262 million in respect of interest paid to the Parent on deposits and subordinated liabilities (year ended 31 December 2012: £504 million).

Refer to note 2 for the impact of changes in the Group's transfer pricing methodology on interest expense in relation to deposits from banks.

4 Fee and commission income and expense

Fee and commission income	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
ATM service fees	59	58
Insurance commissions	7	32
Banking fees and other commissions	28	29
Foreign exchange and credit card	19	21
Other	5	2
Fee and commission income	**118**	**142**
Amounts include:		
Fee and commission income from Parent	3	-

Fee and commission expense	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Fee and commission expense	101	97
Other fees paid to the Parent	11	10
Fee and commission expense	**112**	**107**

Changes to the structure of the Group's contracts with its insurance providers during 2012 and 2013 has resulted in changes in the presentation of various line items within net fee and commission income. This has resulted in lower insurance commissions reported in 2013 compared to 2012, with correspondingly lower insurance fees and commissions expense year on year.

5 Net trading income

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Financial assets designated at fair value through profit or loss	22	11
Financial liabilities designated at fair value through profit or loss	(22)	(9)
Derivatives held for trading	-	4
Foreign exchange transaction gains less losses	-	(4)
Net trading income	**-**	**2**
Amounts include:		
Net trading income / (expense) from Parent	21	(5)

Financial assets designated at fair value through profit or loss relate to a certain number of loans with the Parent designated at fair value, whose return is based on moves in various external indices. These deals represent transactions, booked to hedge the risk on a certain number of customer accounts, which represent financial liabilities designated at fair value through profit and loss.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:34 Page 95

6 Other operating income

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Other operating income	1	(7)
Other operating income	**1**	**(7)**
Amounts include:		
Group share of JCO income (note 18)	-	(2)

7 Operating expenses

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Administrative expenses		
Staff costs (a)		
- Wages and salaries	20	16
- Social security	2	2
- Other staff costs	1	1
- Other pension costs	4	2
Total staff costs	**27**	**21**
- Other administrative expenses (b)	51	69
- Other administrative expenses – related parties (c)	189	174
Amortisation on intangible assets	7	8
Total operating expenses	**274**	**272**
Amounts include		
Group share of JCO costs (note 18)	4	1

(a) Staff costs

Staff costs of £27 million (year ended 31 December 2012: £21 million) include all gross salaries, related social security costs, and pension contributions, attributable to those employees directly employed by the Group or seconded to the Group by the Parent under a secondment agreement. The average number of staff (full time equivalents) was 380 (year ended 31 December 2012: 295). Refer to note 33 for details on compensation paid to key management personnel.

As a result of an organisational structure review of the Group and effected in October 2012, a number of key staff involved in distribution, product provision and risk management activities were transferred to the Group with a consequential year on year increase in staff costs and a corresponding net reduction in other administrative expenses.

(b) Other administrative expenses includes a charge of £17 million (year ended 31 December 2012: £24 million) in respect of the FSCS levy. Of this, £2 million relates to the actual interest rates applied in the period being different from the estimate used to calculate the December 2012 provision. The charge of £24 million in the previous year included amounts due in respect of levies due by the Group for the years ended 31 December 2011 and 31 December 2012.

Included within other administrative expenses is a charge of £nil in respect of a provision for potential payment protection insurance refunds (PPI) (year ended 31 December 2012: £3 million). Refer to note 24 for further details.

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

7 Operating expenses (continued)

(c) Other administrative expenses – Related parties

Other administrative expenses are the costs incurred by the Group in relation to services provided by the Parent under a number of service level agreements. These comprise services across a number of different activities and areas including, but not restricted to, product design, manufacture, distribution and management, customer service, and IT. Included within this management charge is the cost of a number of employees, who carry out services for the Group on behalf of the Parent. These employees' employment contracts are with the Parent and their remuneration is included in the Parent's financial statements. Due to the nature of the services provided it is neither possible to ascertain separately the element of the management charge that reflects the employee staff charge, nor disclose separately employee numbers relevant to the Group's activities.

8 Auditors' remuneration

	Year ended 31 December 2013 £000's	Year ended 31 December 2012 £000's
Fees payable for the audit of the Bank and Group financial statements	441	474
Audit of the Bank's subsidiaries pursuant to legislation	107	115
Audit related assurances services	65	36
Auditors' remuneration	**613**	**625**

The Group's Audit Committee has reviewed the level of fees and is satisfied that it has not affected the independence of the auditors. Audit related assurances services consist of fees in connection with accounting matters and regulatory compliance based work. It is the Group's policy to subject all major assignments to a competitive tender process.

9 Impairment charges on financial assets

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Loans and advances to customers (note 17)	125	183
Impairment charges on financial assets	**125**	**183**

10 Share of profit after tax of jointly controlled entity

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
First Rate Exchange Services Holdings Ltd (FRESH)	34	32
Share of profit after tax of jointly controlled entity	**34**	**32**

This represents the Group's 50% share of profit after tax of its joint venture in FRESH with Post Office Limited. This is a jointly controlled entity (JCE) and accounted for using the equity method of accounting.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:34 Page 97

11 Taxation

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Current tax		
Current year credit / (charge)	4	(6)
Reallocation from deferred tax	31	-
Prior year adjustment	3	-
Total current taxation credit / (charge)	**38**	**(6)**
Deferred tax		
Current year credit	-	42
Impact of corporation tax rate change	(5)	-
Reallocation to current tax	(31)	-
Prior year adjustment	2	2
Total deferred taxation credit	**(34)**	**44**
Taxation credit	**4**	**38**

The reconciliation of tax on the profit before taxation, at the standard UK corporation tax rate, to the Group's actual tax credit for the years ended 31 December 2013 and 31 December 2012 is as follows:

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
(Profit) / Loss before tax	**(57)**	**130**
Multiplied by the Standard rate of Corporation tax in UK of 23.25% (2012 24.5%)	(13)	32
Effects of:		
Non allowable expenses	2	-
Share of results of jointly controlled entity after tax in the income statement	8	8
Impact of corporation tax rate change	(5)	(2)
Prior year adjustment	5	2
Other	7	(2)
Taxation credit	**4**	**38**

The effective taxation rate for the year ended 31 December 2013 is a credit of 7% (year ended 31 December 2012: credit of 29%). Excluding the impact of the results of the jointly controlled entity, FRESH, the effective taxation rate was a credit of 17% for the year ended 31 December 2013 (year ended 31 December 2012: credit of 23%).

12 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprises the following balances:

	31 December 2013 £m	31 December 2012 £m
Cash	37	30
Balances at Central Banks	4,088	6,350
Total cash balances applicable	**4,125**	**6,380**
Loans and advances to banks	12,824	27,090
Less: amounts with a maturity of three months or more	(11,031)	(12,315)
Total loans and advances to banks applicable	**1,793**	**14,775**
Total cash and cash equivalents	**5,918**	**21,155**
Due from the Parent	615	13,570

In 2012 net cash and cash equivalents of £778 million was transferred to the Group as part of the common control transactions. Refer to note 37 for further details.

13 Derivative financial instruments

The Group's utilisation, objectives and policies, on managing the risks that arise in connection with derivatives, are included in the Risk Management section, on pages 32 and 54. The notional amounts of certain types of financial instruments do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Group's exposure to credit risk. The derivative instruments become assets or liabilities as a result of fluctuations in market rates or prices relative to their terms.

The Group holds certain derivatives to which hedge accounting is not applied and these are considered to be held for trading in the table below. These include foreign exchange (FX) forward contracts with customers, with a corresponding FX contract to hedge FX risk with the Parent. At 31 December 2012 they also included equity index linked contracts which related to equity warrants held by the Group; these had a £1 million value at 31 December 2012. At 31 December 2013 the Group did not hold any equity index linked contracts.

During December 2013, the Group moved from a gross cash hedging model to a derivatives hedging model, principally for interest rate risk management. As a result, £12.3 billion of balances owed to the Parent and £12.3 billion of balances owed from the Parent were repaid. In place of this, the Group entered into new derivative transactions with the Parent. The Group has applied hedge accounting to these derivatives as set out in more detail below, and consequently these derivatives are classified as held for hedging in the table below.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:34 Page 99

13 Derivative financial instruments (continued)

The notional amounts and fair values of derivative instruments held by the Group are set out in the following tables:

31 December 2013	Contract / notional amount £m	Fair Value Assets £m	Fair Value Liabilities £m
Derivatives held for trading			
Foreign exchange derivatives	460	7	4
Foreign exchange derivatives – with the Parent	461	4	7
Total derivative assets / liabilities held for trading	**921**	**11**	**11**
Derivatives held as fair value hedges			
Interest rate swaps - with the Parent	381	-	-
Derivatives held as cash flow hedges			
Interest rate swaps - with the Parent	864	-	-
Total derivative assets / liabilities held for hedging	**1,245**	**-**	**-**
Total derivative assets / liabilities	**2,166**	**11**	**11**

31 December 2012	Contract / notional amount £m	Fair Value Assets £m	Fair Value Liabilities £m
Derivatives held for trading			
Foreign exchange derivatives	531	6	3
Equity index linked contracts held	7	1	-
Foreign exchange derivatives – with the Parent	531	3	6
Total derivative assets / liabilities held for trading	1,069	10	9

As set out in the risk management policy on page 32, the Group uses netting arrangements and collateral agreements to reduce its exposure to credit losses. Of the derivative assets of £11 million at 31 December 2013 (31 December 2012: £10 million):

- £4 million (31 December 2012: £3 million) are available for offset against derivative liabilities under CSA and ISDA arrangements. These transactions do not meet the criteria under IAS 32 to enable the assets to be presented net of the liabilities; and
- £7 million (31 December 2012: £7 million) are not covered under CSA and ISDA arrangements or relate to counterparties covered by master netting arrangements with whom a net asset position was held at the balance sheet date. At 31 December 2013, cash collateral of £nil (31 December 2012: £nil) was held against these assets and is reported within Deposits from banks. Refer to note 21.

Placements with other banks includes cash collateral of £3 million (31 December 2012: £nil) placed with derivative counterparties (the Parent) in respect of a net derivative liability position of £3 million (31 December 2012: £2 million).

Hedge accounting
In applying hedge accounting, the Group designates certain derivatives as hedging instruments in either fair value or cash flow hedge relationships.

Fair value hedges
Certain interest rate derivatives are designated as hedging instruments. These are primarily used to reduce the interest rate and foreign exchange exposure on the Group's fixed rate financial assets and liabilities.

Cash flow hedges
The Group designates certain interest rate derivatives in cash flow hedge relationships in order to hedge the exposure to variability in future cash flows arising from floating rate assets.

13 Derivative financial instruments (continued)

The years in which the hedged cash flows are expected to occur are shown in the tables below:

31 December 2013	Up to 1 year £m	1 to 2 years £m	2 to 5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	2	1	8	6	17
Forecast payable cash flows	-	-	-	-	-

The hedged cash flows are expected to impact on the income statement in the following years:

31 December 2013	Up to 1 year £m	1 to 2 years £m	2 to 5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	2	2	8	5	17
Forecast payable cash flows	-	-	-	-	-

During the year ended 31 December 2013 there were no forecast transactions to which the Group had applied hedge accounting which were no longer expected to occur.

14 Loans and advances to banks

	31 December 2013 £m	31 December 2012 £m
Placements with other banks	11,842	26,209
Mandatory deposits with Central Banks	982	881
Loans and advances to banks	**12,824**	**27,090**
Amounts include:		
Due from the Parent	11,646	25,885

Represented in placements with other banks are:

- an amount of £11,646 million (31 December 2012: £25,885 million) arising from transactions with the Parent, which primarily relates to the management of the Group's interest rate risk position. Amounts due to the Parent of £11,651 million (31 December 2012: £25,737 million) are also disclosed in note 21. From a counterparty credit risk perspective, whilst these two amounts are disclosed on a gross basis, the Group has in place a contractual Master Netting Agreement with the Parent, whereby, in the event of default of either party, all amounts due or payable will be settled immediately on a net basis; and
- included within amounts due from the Parent are £337 million of loans, whose return is dependent on movements in various external indices (31 December 2012: £374 million). These loans are designated at fair value through the profit or loss. Refer to note 31 for details on fair value.

During the year ended 31 December 2013, £12.3 billion of balances were repaid by the Parent. For further details see note 33.

Represented in mandatory deposits with Central Banks are:

- an amount of £946 million relating to collateral with Bank of England in respect of notes in circulation (31 December 2012: £858 million). £518 million of this refers to non interest bearing collateral; and
- an amount of £36 million in relation to mandatory cash ratio deposits, which are non-interest bearing deposits placed with the Bank of England under the provisions of the Bank of England Act 1998 (31 December 2012: £23 million).

15 Available for sale financial assets

	31 December 2013 £m	31 December 2012 £m
Government bonds	143	146
Debt securities listed	338	194
Equity securities listed	1	1
Available for sale financial assets	**482**	**341**

At 31 December 2013 and at 31 December 2012, no available for sale financial assets were pledged in sale and repurchase agreements.

The movements on available for sale financial assets are analysed as follows:	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
At 1 January	341	1,543
Revaluation, exchange and other adjustments	(5)	1
Additions	167	360
Disposals	-	(1,282)
Redemptions	(19)	(280)
Amortisation	(2)	(1)
At 31 December	**482**	**341**

16 Loans and advances to customers

	31 December 2013 £m	31 December 2012 £m
Loans and advances to customers	17,844	17,996
Finance leases and hire purchase receivables (see below)	803	717
Gross loans and advances to customers	**18,647**	**18,713**
Less: allowance for impairment charges on loans and advances to customers (note 17)	(719)	(695)
Loans and advances to customers	**17,928**	**18,018**
Amounts include:		
Due from the Parent	7	4

The movement in loans and advances to customers reflects:

- decreases in the commercial lending portfolio of £0.6 billion, primarily reflecting GB Business Banking deleveraging; offset by
- a net increase in residential mortgages arising from the acquisition of a number of mortgage portfolios from the Parent with a total loan value of £1.46 billion for consideration of £1.31 billion (representing a weighted average price of 90%). Included within the discount were both expected credit losses and the differential between the customer interest rates on the assets and current market interest rates for similar assets; and
- excluding mortgage acquisitions, other mortgage lending fell by £0.8 billion, representing £0.9 million of new loans through the Post Office and NI brands which were more than offset by repayments on the overall mortgage portfolio.

Loans and advances to customers include a portion of mortgages which were pledged under the BOE Funding for Lending Scheme.

16 Loans and advances to customers (continued)

Finance leases and hire purchase receivables

Loans and advances to customers include finance leases and hire purchase receivables, which are analysed as follows:

	31 December 2013 £m	31 December 2012 £m
Gross investment in finance leases:		
Not later than 1 year	318	297
Later than 1 year and not later than 5 years	564	494
Later than 5 years	1	1
	883	**792**
Unearned future finance income on finance leases	(80)	(75)
Net investment in finance leases	**803**	**717**
The net investment in finance leases is analysed as follows:		
Not later than 1 year	289	269
Later than 1 year and not later than 5 years	513	447
Later than 5 years	1	1
	803	**717**

The Group's material leasing arrangements include the provision of installment credit and leasing finance for both consumer and business customers.

At 31 December 2013, the accumulated allowance for uncollectable minimum lease payments receivable was £nil (31 December 2012: £nil).

Securitisations

At 31 December 2013, loans and advances to customers include £5,481 million (31 December 2012: £6,197 million) of residential mortgage balances that have been securitised but not derecognised. Refer to note 36. The assets, or interest in the assets were transferred to a Special Purpose Entity (SPE), namely Bowbell no 1 plc, which issued securities to the Group. These are capable of being pledged to monetary authorities, or used as security to secure external funding. None of these securities were pledged or used to secure funding at 31 December 2013 or 31 December 2012. Refer to note 36 for further details.

17 Impairment provisions

The following shows the movement in the impairment provisions during the year ended 31 December 2013 and 31 December 2012:

2013	**Residential mortgages £m**	**Non property SME and corporate £m**	**Property and construction £m**	**Consumer £m**	**Total impairment provisions £m**
Provision at 1 January 2013	44	104	511	36	695
Transfer between provisions	-	17	(17)	-	-
Exchange adjustments	-	-	2	-	2
Provisions utilised	(7)	(28)	(69)	(23)	(127)
Recoveries	-	-	1	5	6
Other movements	(3)	4	16	2	19
Charge to the income statement[1]	7	34	69	14	124
Provision at 31 December 2013	**41**	**131**	**513**	**34**	**719**

2012	Residential mortgages £m	Non property SME and corporate £m	Property and construction £m	Consumer £m	Total impairment provisions £m
Provision at 1 January 2012	33	56	479	26	594
Provisions transfer on acquisition of NIIB on 18 January 2012	-	3	-	14	17
Transfer between provisions	-	35	(35)	-	-
Exchange adjustments	-	-	(2)	-	(2)
Provisions utilised	(8)	(21)	(66)	(28)	(123)
Recoveries	-	-	2	4	6
Other movements	1	2	11	2	16
Charge to the income statement[1]	18	29	122	18	187
Provision at 31 December 2012	44	104	511	36	695

[1] *Presented gross of mortgage indemnity guarantee insurance.*

18 Interest in jointly controlled entity

Jointly controlled entity (JCE)

The Group owns 50% of the shares in First Rate Exchange Services Holdings Limited (FRESH), a company incorporated in Great Britain which provides services in foreign exchange.

The table below shows the movement in the Group's interest in FRESH which is accounted for using the equity method of accounting during the year ended 31 December 2013 and 31 December 2012.

	31 December 2013 £m	31 December 2012 £m
At 1 January	54	62
Share of profit after taxation (note 10)	34	32
Dividends received	(33)	(40)
At 31 December	**55**	**54**

The following amounts represent the Group's 50% share of the revenue and expenses and assets and liabilities of FRESH for the year ended 31 December 2013 and the year ended 31 December 2012.

	31 December 2013 £m	31 December 2012 £m
Revenue	65	63
Expenses	(22)	(21)
Profit before tax	**43**	**42**
Taxation charge	(9)	(10)
Profit after tax	**34**	**32**
Non-current assets	4	3
Current assets	176	126
Total assets	**180**	**129**
Current liabilities	(125)	(75)
Total liabilities	**(125)**	**(75)**
Net assets	**55**	**54**

Jointly controlled operation (JCO)

On 31 August 2012 the Group entered into a new joint arrangement with Post Office Limited. This is a jointly controlled operation but not a separate legal entity. The Group combines its share of the JCO's individual income and expenses, assets and liabilities and cash flows on a line-by-line basis. The amounts relating to the JCO are shown separately in notes 6, 7, 20 and 23.

19 Intangible assets

2013	**Computer software externally purchased £m**	**[1]Computer software internally generated £m**	**[2]Other externally purchased intangible assets £m**	**Total £m**
Cost				
At 1 January 2013	7	34	73	114
Additions	1	-	2	3
Disposals / write-offs	(8)	-	-	(8)
At 31 December 2013	**-**	**34**	**75**	**109**
Accumulated amortisation				
At 1 January 2013	(5)	(23)	(34)	(62)
Disposals / write down	6	-	-	6
Charge to the income statement (note 7)	(1)	(3)	(3)	(7)
At 31 December 2013	**-**	**(26)**	**(37)**	**(63)**
Net book value at 31 December 2013	**-**	**8**	**38**	**46**

2012	Computer software externally purchased £m	Computer software internally generated £m	Other externally purchased intangible assets £m	Total £m
Cost				
At 1 January 2012	8	34	71	113
Additions	-	-	2	2
Disposals / write-offs	(1)	-	-	(1)
At 31 December 2012	7	34	73	114
Accumulated amortisation				
At 1 January 2012	(4)	(19)	(31)	(54)
Charge to the income statement (note 7)	(1)	(4)	(3)	(8)
At 31 December 2012	(5)	(23)	(34)	(62)
Net book value at 31 December 2012	2	11	39	52

Intangible assets have been reviewed for any indication that impairment may have occurred. Where any such indication exists, impairment has been measured by comparing the carrying value of the intangible asset to its recoverable amount. There was no impairment identified in the year ended 31 December 2013 or 31 December 2012.

Some of the assumptions in the calculation of the recoverable amount are subject to uncertainty and are sensitive to changes; for example in the discount rate assumptions or new business volumes and income. In testing for impairment, management notes that a possible break even scenario would be if the following assumptions were used:

- If the income was reduced by 20%: and
- Costs increased by 10%

[1] *Includes £34 million of Deposit System Software, with a remaining amortisation period of 2 years.*
[2] *Includes £71 million of Intangible asset, with a remaining amortisation period of 10 years.*

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

20 Other assets

	31 December 2013 £m	31 December 2012 £m
Sundry and other receivables	24	29
Interest receivable	42	62
Accounts receivable and prepayments	44	42
Other assets	**110**	**133**
Amounts include:		
Group share of JCO assets (note 18)	2	8
Due from the Parent	32	58
Maturity profile of other assets		
Within 1 year	67	99
After 1 year	43	34

21 Deposits from banks

	31 December 2013 £m	31 December 2012 £m
Deposits from banks	11,660	25,742
Deposits from banks	**11,660**	**25,742**
Amounts include:		
Due to the Parent	11,651	25,737

Amounts due to the Parent of £11,651 million (31 December 2012: £25,737 million) relates to borrowings in place to fund and manage interest rate risk on the Group's assets. Refer to note 14 for details of amounts due from the Parent, and note 33 in respect of changes in these balances during 2013.

22 Customer accounts

	31 December 2013 £m	31 December 2012 £m
Term deposits	10,005	12,450
Demand deposits	8,331	8,501
Interest bearing current accounts	785	989
Non interest bearing current accounts	1,736	1,335
Customer accounts	**20,857**	**23,275**
Amounts include:		
Due to entities controlled by the Parent	18	114

Term deposits include deposits of £337 million (31 December 2012: £374 million), whose return is dependent on movements in various external indices; these deposits are designated at fair value through profit or loss. Refer to note 31 for details on fair value.

23 Other liabilities

	31 December 2013 £m	31 December 2012 £m
Accrued interest payable	133	227
Notes in circulation	826	759
Sundry payables	87	95
Accruals and deferred income	12	19
Other liabilities	**1,058**	**1,100**
Amounts include:		
Group share of JCO liabilities (note 18)	7	12
Due to the Parent	24	33
Maturity profile of other liabilities		
Payable within 1 year	1,057	1,095
Payable after 1 year	1	5

The Parent was previously authorised to issue banknotes in Northern Ireland under the Banking Act 2009. From 15 May 2012, under the Bank of Ireland (UK) plc Act 2012, that authority to issue banknotes and the liability for existing banknotes issued by the Parent in Northern Ireland transferred to the Bank. Refer to note 37 for further details.

24 Provisions

	31 December 2013			31 December 2012		
	Payment protection insurance £m	Financial services compensation scheme £m	Total £m	Payment protection insurance £m	Financial services compensation scheme £m	Total £m
At 1 January	3	19	22	1	-	1
Transferred on acquisition of NIIB (note 37)	-	-	-	1	-	1
Charge to the income statement	-	17	17	3	19	22
Utilised during the year	(2)	(13)	(15)	(2)	-	(2)
At 31 December	**1**	**23**	**24**	**3**	**19**	**22**
Expected utilisation period						
Used within 1 year	1	15	16	2	13	15
Used after 1 year	-	8	8	1	6	7

Payment protection insurance (PPI)

As at 31 December 2013, the Group is holding a provision of £1 million (year ended 31 December 2012: £3 million) to cover potential customer claims for refunds of premiums associated with the alleged mis-selling of PPI policies. The provision is based upon known pipeline cases and the expectation of future claims. The closing provision represents managements' best estimate of expected costs.

Financial services compensation scheme (FSCS)

The FSCS is the UK's independent statutory compensation fund for customers of authorised financial services firms and pays compensation if a firm is unable to pay claims against it. The FSCS is funded by levies on the industry. Following the default of a number of financial institutions, the FSCS borrowed funds from HM Treasury to cover compensation in relation to protected deposits. The FSCS recovers the interest cost and capital repayments, together with on-going management expenses, by way of annual levies on member firms. If the assets of the failed institutions are insufficient to repay the Government loan, additional levies may become payable in future periods. The provisions at 31 December 2013 represents the Group's estimate of levies due for the year ended 31 December 2013 and 31 December 2012, less payments made to date.

25 Retirement benefit obligations

The Group's employees and their membership of a particular pension scheme is dependent on their specific employment contract. Where an employee is seconded directly to the Group, the Group only incurs the cost of the contribution to those particular schemes. The Group does not have any liability for payment or increase to pension contributions arising from any historic or future shortfall in the pension assets relative to the pension liabilities of the BoI Group operated schemes. This is stated in an agreement between the Bank and its Parent. Consequently, the schemes have been accounted for as defined contribution scheme in these financial statements and where applicable will be included within the disclosures for defined benefit schemes within the financial statements of BoI Group.

For all employees directly employed by the Group, either through its subsidiaries or directly by the Bank, these employees participate in one of the following schemes.

NIIB defined benefit scheme (NIIB Group Ltd (1975) Pension Scheme)

The NIIB defined benefit scheme is based on final pensionable pay and operates for eligible employees of certain BoI Group companies. Contributions by NIIB and the employees are invested in a trustee-administered fund. As the scheme's underlying assets and liabilities are identifiable as those of the Group the scheme has been accounted for as a defined benefit scheme (as set out in the accounting policy for pension obligations) and the disclosures set out in the remainder of this note relate to this scheme.

In determining the level of contributions required to be made to the scheme and the relevant charge to the income statement the Group has been advised by independent actuaries, Towers Watson.

The scheme is closed to new members.

Life Balance 2 benefit scheme

There are no disclosures applicable in relation to the Life Balance 2 scheme as amounts are too small for presentation.

Regulatory Framework

The NIIB scheme operates under the UK regulatory framework. Benefits are paid to members from a trustee-administered fund. The trustees are responsible for ensuring that the plan is sufficiently funded to meet current and future benefit payments. If plan experience is worse than expected, the Group's obligations are increased.

Under UK pensions legislation, the trustees must agree a funding plan with the Group such that any funding shortfall is expected to be met by additional contributions and investment outperformance. In order to assess the level of contributions required, triennial valuations are carried out with the scheme's obligations measured using prudent assumptions (relative to those used to measure accounting liabilities).

The trustees' other duties include managing the investment of plan assets, administration of plan benefits and exercising of discretionary powers. The Group works closely with the trustees to manage the plan.

Actuarial valuation of the NIIB scheme

A formal valuation of the NIIB scheme has been carried out as at 1 May 2013. The funding method used measures liabilities taking account of the projected future levels of pensionable earnings at the time of commencement of benefits i.e. at normal retirement date. Discussions in relation to the valuation are still ongoing but a schedule of contributions and recovery plan, setting out how any shortfall in the scheme will be met, must be agreed between the trustees and the Group and submitted to the Pensions Regulator by 31 July 2014.

The impact of the scheme's funding position on the future contribution rates of the Group has therefore not been determined at the balance sheet date. In the meantime, the Bank continues to make additional contributions of £0.9 million per annum until 2015 to meet the shortfall in the Scheme of £4.8 million, which was disclosed after the most recently completed triennial valuation as at May 2010.

UK BOI Annual Report 2013_UK BOI Annual Report 20/03/2014 14:06 Page 109

25 Retirement benefit obligations (continued)

Plan details

The following table sets out details of the membership of the NIIB Scheme.

Plan details at last valuation date	By number	By % of funding liability[1]
Scheme Members		
Active	69	32%
Deferred	134	38%
Pensioners	50	30%

[1] *These figures are based on preliminary valuation results and may not reflect the final results once the valuation has been agreed*

Financial and demographic assumptions

The assumptions used in calculating the accounting costs and obligations of the NIIB Scheme, as detailed below, are set by the Directors after consultation with Towers Watson.

The discount rate used to determine the present value of the obligations is set by reference to market yields on high quality corporate bonds. The assumption for RPI price inflation is set by reference to the difference between yields on longer-term conventional government bonds and index-linked bonds with an appropriate adjustment to reflect distortions due to supply and demand. The assumption for CPI inflation is set by reference to RPI inflation, with an adjustment applied, as no CPI linked bonds exist.

The salary assumption takes into account inflation, seniority, promotion and current employment market relevant to the Group.

The financial assumptions used in measuring the Group's defined benefit liability under IAS 19 are set out in the table below.

Financial assumptions	**31 December 2013 % p.a.**	31 December 2012 % p.a.
Consumer price inflation	2.70	2.40
Retail price inflation	3.60	2.90
Discount rate	4.45	4.60
Rate of general increase in salaries	4.10	3.40
Rate of increase in pensions in payment	3.25	2.85
Rate of increase in to deferred pensions	2.70	2.40

25 Retirement benefit obligations (continued)

Mortality Assumptions

The mortality assumptions adopted are outlined in the table below.

Post retirement mortality assumptions	31 December 2013 Years	31 December 2012 Years
Longevity at age 70 for current pensioners		
Men	18.2	18.1
Women	20.5	20.4
Longevity at age 60 for active members currently aged 60 years		
Men	28.3	28.1
Women	30.6	30.4
Longevity at age 60 for active members currently aged 40 years		
Men	32.2	32.0
Women	33.9	33.7

Amounts recognised in financial statements

The table below outlines where the Group's defined benefit plans are recognised in the financial statements

	31 December 2013 £m	31 December 2012 £m
Total charge in operating expenses	**(1)**	**(1)**
Total gain / (loss) in remeasurements[1]	**1**	**(1)**
Total liability in the balance sheet	**-**	**2**

[1] *Shown before deferred tax*

25 Retirement benefit obligations (continued)

The movement in the net defined benefit obligation in respect of the NIIB Scheme is as follows:

	Present value of obligation £m	Fair value of plan assets £m	(Surplus) / deficit of plan £m
At 1 January 2013	**23**	**(21)**	**2**
Current service cost	1	-	1
Interest expense / (income)	1	(1)	-
Total amount in recognised income statement	**2**	**(1)**	**1**
Return on plan assets not included in income statement	-	(2)	(2)
Change in financial assumptions	2	-	2
Experience (gains) / losses	(1)	-	(1)
Total remeasurements in other comprehensive income	**1**	**(2)**	**(1)**
Employer contributions	-	(2)	(2)
Benefit payments	(1)	1	-
Other movements	**(1)**	**(1)**	**(2)**
At 31 December 2013	**25**	**(25)**	**-**
At 1 January 2012	21	(19)	2
Interest expense / (income)	1	(1)	-
Total amount recognised in the income statement	1	(1)	-
Return on plan assets not included in the income statement	-	(1)	(1)
Change in financial assumptions	1	-	1
Total remeasurements in other comprehensive income	1	(1)	-
Employer contributions	-	(1)	(1)
Benefit payments	-	1	1
Other movements	-	-	-
At 31 December 2012	23	(21)	2

Asset breakdown	**31 December 2013 £m**	31 December 2012 £m
Equities (quoted)	15	12
Index linked government bonds (quoted)	10	8
Cash (quoted)	-	1
Total fair value of assets	**25**	**21**

25 Retirement benefit obligations (continued)

Sensitivity of defined benefit obligation to key assumptions

The table below sets out how the defined benefits obligation would have been affected by changes in the significant actuarial assumptions that were reasonably possible at 31 December 2013:

Impact on defined benefit obligation	Change in assumptions	Increase in assumptions £m	Decrease in assumptions £m
Discount rate	0.25%	(1.3)	1.4
Inflation[1]	0.1%	0.5	(0.5)
Salary growth	0.1%	-	-
Life expectancy	1 year	0.6	(0.6)

[1] *including other inflation-linked assumptions (CPI inflation, pension increases, salary growth)*

Some of the above changes in assumptions may have an impact on the value of the scheme's investment holdings. For example, the plan holds a proportion of its assets in index-linked bonds. A fall in the rate of inflation would be expected to lead to an reduction in the value of these assets, thus partly offsetting the reduction in the defined benefit obligation. The extent to which these sensitivities are managed is discussed further below.

Future cash flows

The plan's liabilities represent a long-term obligation and most of the payments due under the plan will occur several decades into the future.

The duration, or average term to payment for the benefits due, weighted by liability, is c. 23 years.

Expected employer contributions for the year ended 31 December 2014 are £1.3 million. Expected employee contributions for the year ended 31 December 2014 are £43,000.

Years	Benefit payments from Plan assets (£m)
2013-2022	7
2023-2032	14
2033-2042	22
2043-2052	27
2053-2062	24
2063-2072	17
2073-2082	8
2083-2092	2
After 2093	-
	121

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:34 Page 113

25 Retirement benefit obligations (continued)

Risks and risk management

The NIIB scheme has a number of areas of risk. The key areas of risk, and the ways in which the Group has sought to manage them, are set out in the table below.

The risks are considered from both a funding perspective, which drives the cash commitments of the Group, and from an accounting perspective, i.e. the extent to which such risks affect the amounts recorded in the Group's financial statements.

Risk	Description
Asset volatility	The funding liabilities are calculated using a discount rate set with reference to government bond yields, with allowance for additional return to be generated from the investment portfolio. The defined benefit obligation in the Group's financial statements is calculated using a discount rate set with reference to high quality corporate bond yields. The plan holds a significant proportion of its assets in equities and other return-seeking assets. The returns on such assets tend to be volatile and are not correlated to government bonds. This means that the funding level is likely to be volatile in the short-term, potentially resulting in short-term cash requirements and an increase in the net defined benefit liability recorded on the balance sheet.
Changes in bond yields	Interest rate and inflation risks, along with equity risk, are the scheme's largest risks. From an accounting liability perspective, the scheme is also exposed to movements in corporate bond spreads. The scheme uses an investment in index-linked bonds to manage its interest rate and inflation risk. This portfolio is used to broadly hedge against movements in long-term interest rates and inflation expectations. The portfolio does not completely eliminate risk and only addresses a portion of the scheme's interest rate and inflation risks. Furthermore, it does not hedge against changes in the credit spread available on corporate bonds used to derive the accounting liabilities. The investment in index-linked bonds offers a degree of matching, i.e. the movement in assets arising from changes in bond yields partially matches the movement in the funding or accounting liabilities. In this way, the exposure to movements in bond yields is reduced.
Inflation risk	The majority of the scheme's benefit obligations are linked to inflation and higher inflation will lead to higher liabilities, although in most cases caps on the level of inflationary increases are in place to protect the plan against inflation.
Life expectancy	The majority of the plan's obligations are to provide a pension for the life of the member, which means that increases in life expectancy will result in an increase in the plan's liabilities.

26 Deferred tax

	31 December 2013 £m	31 December 2012 £m
The movement on the deferred tax account is as follows:		
At 1 January	74	26
Income statement (charge) / credit for year (note 11)	(34)	44
Losses transferred from Parent	86	-
Available for sale securities - transferred to reserves	1	-
Other movements	1	4
At 31 December	**128**	**74**

Deferred tax assets and liabilities are attributable to the following items:

	31 December 2013 £m	31 December 2012 £m
Deferred tax assets		
Unutilised tax losses	117	66
Available for sale securities	1	-
Leased assets	8	6
Other	3	3
Total deferred tax assets	**129**	**75**
Deferred tax liabilities		
Fixed assets	(1)	(1)
Total deferred tax liabilities	**(1)**	**(1)**
Represented on the balance sheet as follows:		
Deferred tax assets	128	74
Total deferred tax	**128**	**74**

During the period, the Group reassessed the value of losses acquired from its ultimate Parent undertaking on the transfer of business assets in 2010, and consequently has recognised an asset of £86 million in respect of the taxation benefit of losses transferred from the Parent. The Group did not provide any consideration for the losses and, therefore, this amount is being treated as a capital contribution received.

26 Deferred tax (continued)

The deferred tax credit in the income statement comprises the following temporary differences:

	31 December 2013 £m	31 December 2012 £m
Current year losses	-	40
Impact of corporation tax rate change	(5)	(2)
Fixed and leased assets	1	2
Other	(1)	2
Reallocation to current tax	(31)	-
Prior year adjustment	2	2
Total deferred tax	**(34)**	**44**

The UK Government announced that the main rate of corporation tax would reduce to 21% from 1 April 2014 to be followed by further reductions to 20% for the year beginning 1 April 2015. The reduction in the corporation tax rate to 20% from 1 April 2015 was substantively enacted at the balance sheet date and the effect of this change has been to reduce the deferred tax asset at 31 December 2013 by £5 million. Refer to note 11.

27 Subordinated liabilities

	31 December 2013 £m	31 December 2012 £m
£523 million subordinated floating rate loans 2020[1]	523	523
£90 million subordinated floating rate loans 2022[2]	90	90
£45 million subordinated floating rate loans 2022[3]	45	45
Subordinated liabilities	**658**	**658**

These liabilities constitute unsecured obligations of the Group to its Parent, subordinated in right of payments to the claim of depositors, and other unsubordinated creditors of the Group. The subordinated liabilities meet the definition of a financial liability as the Group does not have an unconditional right to avoid the repayment of the principal or interest. Therefore, the liabilities are recognised on the balance sheet at amortised cost, using the effective interest method.

All of the current notes are redeemable in whole but not in part, subject to the prior approval of the PRA, on the fifth anniversary of their drawdown date. In the event of a wind up of the Group, the loans will become immediately due and payable without demand, together with all interest accrued thereon.

[1] *Initial call date 7 October 2015. If not prepaid at this point, they are due in full on their final maturity date of 7 October 2020. They bear interest at a floating rate of 6.5% per annum above the sterling LIBOR six month rate.*
[2] *Initial call date 21 July 2017. If not prepaid at this point, they are due in full on their final maturity date of 21 July 2022. They bear interest at a floating rate of 11% per annum above the sterling LIBOR six month rate.*
[3] *Initial call date 21 December 2017. If not prepaid at this point, they are due in full on their final maturity date of 21 December 2022. They bear interest at a floating rate of 9% per annum above the sterling LIBOR six month rate.*

28 Contingent liabilities and commitments

The table below gives the contractual amounts of contingent liabilities and commitments. The maximum exposure to credit loss under contingent liabilities and commitments is the contractual amount of the instrument in the event of non-performance by the other party where all counter claims, collateral, or security prove worthless.

	31 December 2013 Contractual amount £m	31 December 2012 Contractual amount £m
Contingent liabilities		
Guarantees and irrevocable letters of credit	15	14
Other contingent liabilities	8	9
Total contingent liabilities	**23**	**23**
Commitments		
Undrawn formal standby facilities, credit lines and other commitments to lend		
- revocable or irrevocable with original maturity of 1 year or less	3,008	3,162
- irrevocable with original maturity of over 1 year	217	232
Total commitments	**3,225**	**3,394**

Guarantees and letters of credit are given as security to support the performance of a customer to third parties. As the Group will only be required to meet these obligations in the event of the customer's default, the cash requirements of these instruments are expected to be considerably below their nominal amounts.

Other contingent liabilities primarily include performance bonds and are generally short term commitments to third parties which are not directly dependent on the customer's credit worthiness. Documentary credits commit the Group to make payments to third parties, on production of documents, which are usually reimbursed immediately by customers.

Commitments to lend are agreements to lend to a customer in the future, subject to certain conditions.

29 Share capital

Movements in issued ordinary and preference shares	Ordinary[1] Shares 31 December 2013 £m	Ordinary[1] Shares 31 December 2012 £m	Preference[1] Shares 31 December 2013 £m	Preference[1] Shares 31 December 2012 £m
At 1 January	816	756	300	300
Issued during the year	35	60	-	-
At 31 December	**851**	**816**	**300**	**300**

[1] *All shares issued are in denominations of £1, therefore the table above also represents unit values.*

At 31 December 2013 and at 31 December 2012, all ordinary and preference shares issued by the Group were held by the Parent.

All ordinary and preference shares issued were fully paid at 31 December 2013 and 31 December 2012.

Ordinary shares
- In April 2013, 35 million units of ordinary shares at a par value of £1 each were acquired by the Parent.
- In September 2012, 10 million units of ordinary shares at a par value of £1 each were acquired by the Parent.
- In December 2012, 50 million units of ordinary shares at a par value of £1 each were acquired by the Parent.

Preference shares
On 31 March 2013 the second non-cumulative preference dividend fell due; this was not paid as the terms and conditions were not met.

The terms and conditions attaching to the preference shares are outlined below:
- the preference shares are perpetual, with an option by the Group to redeem them at 31 March 2016 and at any dividend payment date thereafter, subject to approval from the PRA and compliance with the Companies Act 2006;
- dividends are payable annually in arrears at a rate of 13% and are payable unfettered at the discretion of the Group, subject to approval from the PRA and compliance with the Companies Act 2006; and
- the holders of preference shares shall not be entitled to receive notice of, or to attend or vote at, any general meeting of the Group.

On a winding-up or other return of capital of the Group, the assets of the Group available to the shareholder shall be applied in priority to any payment to the holders of ordinary shares and any other class of shares in the capital of the Group then in issue, ranking junior to the Preference Shares on such return of capital and pari passu on such return of capital with the holders of any other class of shares in the capital of the Group then in issue.

Distribution upon winding up will be a sum equal to the aggregate of:
(a) an amount equal to dividends accrued thereon for the then current dividend period to the date of the commencement of the winding-up or other such return of capital; and
(b) an amount equal to £1 per Preference Share.

30 Liquidity risk

The tables below summarise the maturity profile of the Group's financial liabilities, at 31 December 2013 and at 31 December 2012, based on contractual undiscounted repayment obligations. See also Risk management section 3.1 for details of the maturity of assets and liabilities on a discounted basis.

The Group does not manage liquidity risk on the basis of contractual maturity. Instead, the Group manages liquidity risk based on expected cash flows. The balances will not agree directly to the balance sheet because the table incorporates all cash flows, on an undiscounted basis, related to both principal and interest payments.

Customer accounts include a number of term accounts that contain easy access features. These allow the customer to access a portion or all of their deposit notwithstanding that this repayment could result on a financial penalty being paid by the customer. For such accounts the portion subject to the potential early access has been classified accordingly in the table below as 'demand'.

31 December 2013	**Demand £m**	**Up to 3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Deposits from banks	645	35	6,329	4,722	151	11,882
Customer accounts	12,331	3,672	3,529	1,397	-	20,929
Subordinated liabilities	-	5	49	245	839	1,138
Contingent liabilities	23	-	-	-	-	23
Commitments	3,008	-	-	217	-	3,225
Total	**16,007**	**3,712**	**9,907**	**6,581**	**990**	**37,197**

31 December 2012	Demand £m	Up to 3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Deposits from banks	1,807	18,992	1,746	3,286	177	26,008
Customer accounts	12,353	10,089	728	208	1	23,379
Subordinated liabilities	-	5	51	217	889	1,162
Contingent liabilities	23	-	-	-	-	23
Commitments	3,162	-	-	232	-	3,394
Total	17,345	29,086	2,525	3,943	1,067	53,966

The table below summarises the maturity profile of the Group's derivative liabilities. The Group manages liquidity risk based on expected cash flows, therefore the undiscounted cash flows payable on derivatives liabilities are classified according to their contractual maturity.

31 December 2013	**Demand £m**	**Up to 3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Gross settled derivative liabilities - outflows	-	(318)	(142)	(10)	-	(470)
Gross settled derivative liabilities - inflows	-	311	139	10	-	460
Gross settled derivative liabilities - net flows	-	(7)	(3)	-	-	(10)
Net settled derivative liabilities	-	-	1	1	(3)	(1)
Total derivatives cash flows	**-**	**(7)**	**(2)**	**1**	**(3)**	**(11)**

30 Liquidity risk (continued)

31 December 2012	Demand £m	Up to 3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Gross settled derivative liabilities - outflows	-	(321)	(195)	(28)	-	(544)
Gross settled derivative liabilities - inflows	-	315	192	28	-	535
Gross settled derivative liabilities - net flows	-	(6)	(3)	-	-	(9)
Net settled derivative liabilities	-	-	-	-	-	-
Total derivatives cash flows	-	(6)	(3)	-	-	(9)

31 Measurement basis of financial assets and financial liabilities

The table below analyses the carrying amounts of the financial assets and financial liabilities, by accounting treatment and by balance sheet heading.

	At fair value through profit or loss			At fair value through other comprehensive income (OCI)		
31 December 2013	**Held for trading £m**	**Designated upon initial recognition £m**	**Held for Hedging[1] £m**	**Available for sale £m**	**Held at amortised cost £m**	**Total £m**
Financial assets						
Cash and balances with Central Banks	-	-	-	-	4,125	4,125
Items in the course of collection from other banks	-	-	-	-	182	182
Derivative financial instruments	11	-	-	-	-	11
Loans and advances to banks	-	337	-	-	12,487	12,824
Available for sale financial assets	-	-	-	482	-	482
Loans and advances to customers	-	-	-	-	17,928	17,928
Total financial assets	**11**	**337**	**-**	**482**	**34,722**	**35,552**
Financial liabilities						
Deposits from banks	-	-	-	-	11,660	11,660
Customer accounts	-	337	-	-	20,520	20,857
Items in the course of transmission to other banks	-	-	-	-	94	94
Derivative financial instruments	11	-	-	-	-	11
Subordinated liabilities	-	-	-	-	658	658
Total financial liabilities	**11**	**337**	**-**	**-**	**32,932**	**33,280**

[1] *The amounts relating to derivatives held for hedging are too small for presentation*

31 Measurement basis of financial assets and financial liabilities (continued)

The fair value and contractual amount due on maturity, of financial liabilities designated at fair value upon initial recognition, are shown in the table below.

	31 December 2013		31 December 2012	
	Fair values £m	**Contractual amount due to Maturity £m**	Fair Values £m	Contractual amount due to Maturity £m
Customer accounts	337	333	374	368

31 December 2012	At fair value through profit or loss		At fair value through other comprehensive income (OCI)		
	Held for trading £m	Designated upon initial recognition £m	Available for sale £m	Held at amortised cost £m	Total £m
Financial assets					
Cash and balances with Central Banks	–	-	-	6,380	6,380
Items in the course of collection from other banks	-	-	-	193	193
Derivative financial instruments	10	-	-	-	10
Loans and advances to banks	-	374	-	26,716	27,090
Available for sale financial assets	-	-	341	-	341
Loans and advances to customers	-	-	-	18,018	18,018
Total financial assets	10	374	341	51,307	52,032
Financial liabilities					
Deposits from banks	-	-	-	25,742	25,742
Customer accounts	-	374	-	22,901	23,275
Items in the course of transmission to other banks	-	-	-	173	173
Derivative financial instruments	9	-	-	-	9
Subordinated liabilities	-	-	-	658	658
Total financial liabilities	9	374	-	49,474	49,857

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:35 Page 121

32 Fair value of financial assets and financial liabilities

Fair value of financial assets and financial liabilities
The fair value of a financial instrument is defined as 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.

Where possible, the Group calculates fair value using observable market prices. Where market prices are not available, fair values are determined using valuation techniques which may include discounted cash flow models or comparisons to instruments with characteristics either identical or similar to those of the instruments held by the Group or recent arm's length market transactions. These fair values are classified within a three-level fair value hierarchy, based on the inputs used to value the instrument. Where the inputs might be categorised within different levels of the fair value hierarchy, the fair value measurement in its entirety is categorised in the same level of the hierarchy as the lowest level input that is significant to the entire measurement. The levels are defined as:

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date.

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 inputs are unobservable inputs for the asset or liability.

Transfers between different levels are assessed at the end of all reporting periods.

(a) Financial assets and liabilities held at amortised cost
All financial instruments are initially recognised at fair value. The Group subsequently measures derivatives and available for sale financial assets at fair value in the balance sheet. These instruments are shown as 'at fair value through profit or loss (FVTPL)' or 'at fair value through Other Comprehensive Income (OCI)' in note 31 on the measurement basis of financial assets and liabilities. A description of the methods and assumptions used to calculate fair values of these assets and liabilities is set out below.

Derivative financial instruments
The Group's derivative financial instruments are valued using valuation techniques commonly used by market participants. These consist of discounted cash flow and options pricing models, which typically incorporate observable market data, principally interest rates, basis spreads, foreign exchange rates, equity prices and counterparty credit (level 2 inputs).

Available for sale financial assets
All of the Group's available for sale financial assets trade in an active market; fair value has been determined directly from observable market prices (level 1 inputs).

Loans and advances to banks
Loans and advances to banks designated at fair value through profit or loss consist of loans, which contain an embedded derivative (typically an equity option). These instruments are valued using valuation techniques, which use observable market data (level 2 inputs).

Customer accounts
Customer accounts designated at fair value through profit or loss consist of deposits, which contain an embedded derivative (typically an equity option). These instruments are typically valued using valuation techniques, which use observable market data. The Group incorporates the effect of changes in its own credit spread when valuing these instruments. The Group estimates this spread by reference to recent transactions in the same instrument or in similar instruments issued by the Parent (level 2 inputs).

(b) Financial assets and liabilities not subsequently measured at fair value
For financial assets and liabilities which are not subsequently measured at fair value on the balance sheet, the Group discloses their fair value in a way that permits them to be compared to their carrying amounts. The methods and assumptions used to calculate the fair values of these assets and liabilities are set out below.

32 Fair value of financial assets and financial liabilities (continued)

Loans and advances to banks

The estimated fair value of floating rate placements and overnight placings is their carrying amount. The estimated fair value of fixed interest bearing placements is based on discounted cash flows, using prevailing money market interest rates for assets with similar credit risk and remaining maturity (level 2 inputs).

Loans and advances to customers

Loans and advances to customers are carried net of provisions for impairment. The fair value of both fixed and variable rate loans and advances to customers is estimated using valuation techniques, which include:

- recent arm's length transactions in similar assets (level 2 inputs); and
- the discounting of estimated future cash flows at current market rates, incorporating the impact of current credit spreads and margins. The fair value reflects both loan impairments at the balance sheet date and estimates of market participants' expectations of credit losses over the life of the loans (level 3 inputs).

Deposits from banks and customer accounts

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits and other borrowings without quoted market prices is based on discounted cash flows, using interest rates for new deposits with similar remaining maturity (level 2 inputs).

Subordinated liabilities

As quoted market prices are not available, the fair value is estimated by benchmarking the yield against similar bonds issued by the Parent, which have similar maturity dates (level 2 inputs).

(c) Fair value hierarchy

The following table shows, for the Group's financial assets and financial liabilities that are recognised and subsequently measured at fair value, their classification within a three-level fair value hierarchy.

Level 1 comprises financial assets and financial liabilities valued using quoted market prices in active markets. An active market is one in which transactions occur with sufficient volume and frequency to provide pricing information on an on-going basis.

Level 2 comprises financial assets and financial liabilities valued using techniques based significantly on observable market data.

Level 3 comprises financial assets and financial liabilities valued using techniques where the impact of the non-observable market data is significant in determining the fair value of the instrument. Non-observable market data is not readily available in an active market due to market illiquidity or complexity of the product. These inputs are generally determined based on observable inputs of a similar nature, historic observations on the level of the input, or analytical techniques.

32 Fair value of financial assets and financial liabilities (continued)

31 December 2013	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets held at fair value				
Derivative financial instruments	-	11	-	11
Loans and advances to banks	-	337	-	337
Available for sale financial assets	481	1	-	482
Total financial assets at fair value	**481**	**349**	**-**	**830**
As a % of fair value assets	**58%**	**42%**	**-**	**100%**
Financial liabilities held at fair value				
Customer accounts	-	337	-	337
Derivative financial instruments	-	11	-	11
Total financial liabilities at fair value	**-**	**348**	**-**	**348**
As a % of fair value liabilities	**-**	**100%**	**-**	**100%**

31 December 2013	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets held at amortised cost				
Cash and balances at central banks	4,125	-	-	4,125
Items in the course of collection from other banks	182	-	-	182
Loans and advances to banks	-	12,609	-	12,609
Loans and advances to customers	-	-	17,318	17,318
Total	**4,307**	**12,609**	**17,318**	**34,234**
Financial liabilities held at amortised cost				
Deposits from banks	-	11,701	-	11,701
Customer accounts	-	20,566	-	20,566
items in the course of transmission to other banks	94	-	-	94
Subordinated liabilities	-	694	-	694
Total	**94**	**32,961**	**-**	**33,055**

The Group had no assets or liabilities held at fair value on the balance sheet within level 3 at 31 December 2013 or 31 December 2012. There were also no transfers in or out of level 3 during the year ended 31 December 2013 or 31 December 2012.

32 Fair values of financial assets and financial liabilities (continued)

31 December 2012	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets held at fair value				
Derivative financial instruments	1	9	-	10
Loans and advances to banks	-	374	-	374
Available for sale financial assets	341	-	-	341
Total financial assets at fair value	342	383	-	725
As a % of fair value assets	47%	53%	-	100%
Financial liabilities held at fair value				
Customer accounts	-	374	-	374
Derivative financial instruments	-	9	-	9
Total financial liabilities at fair value	-	383	-	383
As a % of fair value liabilities	-	100%	-	100%

The carrying amount and the fair value of the Group's financial assets and liabilities as at 31 December 2013 and 31 December 2012 are set out in the table below:

	31 December 2013		31 December 2012	
	Carrying amount £m	**Fair values £m**	Carrying amount £m	Fair values £m
Financial Assets				
Cash and balances at Central Banks[1]	4,125	4,125	6,380	6,380
Items in course of collection from other banks[1]	182	182	193	193
Loans and advances to banks	12,824	12,946	27,090	27,230
Available for sale financial assets[1]	482	482	341	341
Derivatives financial assets[1]	11	11	10	10
Loans and advances to customers	17,928	17,318	18,018	16,655
Financial Liabilities				
Deposits from banks	11,660	11,701	25,742	25,907
Customer accounts	20,857	20,903	23,275	23,419
Items in the course of transmission to other banks[1]	94	94	173	173
Derivative financial liabilities[1]	11	11	9	9
Subordinated liabilities	658	694	658	666

[1] *The fair value of these financial instruments is equal to the carrying value. These instruments are either carried at market value or have minimal credit losses, and are either short term in nature or re-priced frequently.*

33 Related party transactions

Parties are considered to be related, if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions, or one other party controls both. The definition includes subsidiaries, jointly controlled entity and the Parent, as well as other key management personnel.

(a) Parent

The Group is a wholly owned controlled subsidiary of The Governor and Company of the Bank of Ireland, a corporation established in Ireland in 1783 under Royal Charter, with a primary listing on the Irish Stock Exchange and a premium listing on the London Stock Exchange. This is the ultimate controlling party of the Group and BoI Group. The results of the Group are consolidated in the Bank of Ireland Group financial statements, which are available at Bank of Ireland, Head Office, 40 Mespil Road, Dublin 4, Ireland.

The Governor and Company of the Bank of Ireland acts as guarantor for Bank of Ireland UK plc in its transactions with the Bank of England. If under any circumstances Bank of Ireland UK plc fails to make payment of guaranteed amounts to the Bank of England or does not perform any of its other obligations under the relevant agreement, the Governor and Company of the Bank of Ireland shall pay the amounts or perform its obligations upon written demand from Bank of England.

The Group receives a range of services from its Parent and related parties, including loans and deposits, forward exchange, interest rate cover and various administrative services. In the course of operating its business, the Group utilises a number of key services from its Parent, which are subject to a number of Service Level Agreements and costs, and these are disclosed in the applicable notes to the financial statements.

In 2012 the Parent applied a standard transfer pricing methodology for all businesses in respect of deposits placed with, or amounts borrowed from, the Parent. A key driver of the transfer price was the date of origination of the relevant customer loan or deposit. When customer loans and deposits transferred to the Group on 1 November 2010, the transfers were at historical carrying values and the relevant transfer pricing also transferred at historical rates. At that time the origination dates for customer deposits transferred was more recent than that for customer loans transferred resulting in a net amount payable to the Group from the Parent as a result of the application of transfer pricing.

In 2013 the Group started to move from the aforementioned legacy transfer pricing method due to the development of its own internal transfer pricing process, which was based on its own deposit funding costs rather than the funding cost of the Parent. It was agreed that the Group would phase off the Parent's transfer pricing funding methodology gradually over the 3 years from 2012-2014. This phase off will therefore result in the net funding income being allocated to the Group from the Parent reducing to nil by 2015.

The relevant net amount payable by the Parent under transfer pricing in respect of the year ended 31 December 2013 was £98 million compared to £176 million for the year ended 31 December 2012, with the changes in methodology outlined above having contributed significantly to this result.

During the year the Group purchased a portfolio of mortgage assets from the Parent for £1.3 billion (year ended 31 December 2012: £3.5 billion). These were measured on initial recognition at fair value. To establish fair value, the Group used a valuation technique, which reasonably reflects how the market could be expected to price the assets, and whose variables include market data. The assets purchased are external to the Group and reflected in loans and advances to customers.

During December 2013, the Group moved from a gross cash hedging model to a derivatives hedging model. As a result, £12.3 billion of balances owed to the Parent and £12.3 billion of balances owed from the Parent were repaid and the Group then entered into new derivative transactions with the Parent.

During the year, the Group reassessed the value of losses acquired from its ultimate parent undertaking on the transfer of business assets in 2010, and consequently has recognised an asset of £86 million in respect of the taxation benefit of losses transferred from the Parent. The Group did not provide any consideration for the losses and, therefore, this amount is treated as being a capital contribution received.

33 Related party transactions (continued)

Summary	31 December 2013 Parent[1] £m	31 December 2012 Parent[1] £m
Income statement		
Interest income	315	616
Interest expense	(262)	(504)
Fee and commission income	3	-
Fees and commissions expense	(11)	(10)
Net trading income / (expense)	21	(5)
Impairment charges on financial assets	(1)	4
Operating expenses paid for services provided[2]	(189)	(174)
Total	**(124)**	**(73)**
Assets:		
Loans and advances to banks	11,646	25,885
Loans and advances to customers	7	4
Other assets	32	58
Derivatives	4	3
Total assets	**11,689**	**25,950**
Liabilities:		
Deposits from banks	11,651	25,737
Customer accounts	18	114
Other liabilities	24	33
Derivatives	7	6
Total liabilities	**11,700**	**25,890**
Net exposure	**(11)**	**60**

(b) Pension funds

The Group provides a range of normal banking and financial services, which are not material to the Group, to various pension funds operated by the BoI Group for the benefit of employees, which are conducted on similar terms to third party transactions.

(c) Irish Government

The Irish Government, through both the Parent's participation in the Irish Credit Institutions (Eligible Liabilities Guarantee) Scheme (the ELG Scheme) and the investment by the Irish National Pension Reserve Fund Commission in the preference stock of the Parent up to 11 December 2013, is a related party of the Group.

On 21 July 2010, the Group elected to participate in the ELG Scheme. The cost of £2 million was borne by the Parent for the year ended 31 December 2013 (year ended 31 December 2012: £15 million). Participation in the ELG scheme is optional; on this basis and in light of the fact that the FSCS is the standard deposit protection scheme in the UK the Group exited this scheme for new deposits on 30 March 2012. The ELG scheme was withdrawn from midnight 28 March 2013 for all participating banks. All existing deposits continue to be covered until their date of maturity.

The Group had no other transactions with the Irish Government during the year ended 31 December 2013, or the year ended 31 December 2012.

[1] This relates to amounts in respect of the Parent and entities controlled by the Parent.
[2] Included within this amount is a fee of £50,000 (year ended 31 December 2012: £25,000) to Archie Kane, Governor and non-executive Director of the Parent who was appointed as consultant advisor to the Group in June 2012.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:35 Page 127

33 Related party transactions (continued)

(d) Transactions with Key Management Personnel

i. Loans to Directors

The following information is presented in accordance with Section 413 of the Companies Act 2006. For the purposes of the Companies Act disclosures, 'Directors' means the Board of Directors and any past Directors who were Directors, during the relevant year.

Companies Act Disclosures **Loans to Directors 2013**	**Balance as at 1 January 2013** **£'000**	**(1) (4) Balance as at 31 December 2013** **£'000**	**(2) (3) Aggregate maximum amount outstanding during the year ended 31 December 2013** **£'000**
Loans to Directors	467	436	467

Companies Act Disclosures Loans to Directors 2012	(5) Balance as at 1 January 2012 £'000	(1) (4) Balance as at 31 December 2012 £'000	(2) (3) Aggregate maximum amount outstanding during the year ended 31 December 2012 £'000
Loans to Directors	891	467	834

All loans to Directors are made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for similar transactions with other persons, unconnected with the Group and of similar financial standing except a credit card and a current account (with overdraft facility) for Executive Directors, which are on terms similar to those available to staff generally. They do not involve more than the normal risk of collectability.

ii. Key management personnel - loans and deposits (IAS 24)

For the purposes of IAS 24 Related Party Disclosures, 'key management personnel' (KMP) comprise the Directors of the Board, the Head of GB Strategic Change and Outsourcing, the Director, Distribution and Marketing UK, the Managing Director and Head of GB Business Banking, the Managing Director of FRESH, the Director of Consumer Banking UK, the HR Director and any past KMP, who was a KMP during the relevant year.

Key management personnel, including Directors, hold products with the Group in the ordinary course of business. All loans to Non-Executive Directors are made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons, and do not involve more than the normal risk of collectability or present other unfavourable features. Loans to KMP, other than Non-Executive Directors, are made on terms similar to those available to staff generally, and / or in the ordinary course of business on normal commercial terms.

[1] *Balance includes principal and interest.*
[2] *These figures include credit card exposures at the maximum statement balance. In all cases, Directors have not exceeded their approved limits. The maximum approved credit limit on any credit card held by key management personnel is £10,000.*
[3] *The maximum amount outstanding was calculated using the maximum balance on each account. The highest maximum outstanding liability, during the year ended 31 December 2013, for any member of key management personnel and their close family did not exceed £458,000 (31 December 2012: £694,000). The closing balance includes interest accrued and interest paid; the maximum balance includes interest paid.*
[4] *Foreign currency amounts are converted to GBP, using exchange rates at 31 December 2013, 31 December 2012 and the average exchange rate for the year, as appropriate.*
[5] *The opening balance includes balances and transactions with Directors who retired during 2011 and were not therefore related parties during 2012.*

33 Related party transactions (continued)

The aggregate amounts outstanding, in respect of all loans, quasi-loans and credit transactions, between the Group, its key management personnel (as defined above) and key management personnel of the Parent, including members of their close families and entities influenced by them are shown in the table below.

2013 **Key management personnel**	**(5) Balance as at 1 January 2013 £'000**	**(1) (4) Balance as at 31 December 2013 £'000**	**(2) (3) Aggregate maximum amounts outstanding during the year ended 31 December 2013 £'000**	**Total number KMP as at 1 January 2013**	**Total number of KMP as at 31 December 2013**
Loans	488	444	487	9	9
Deposits	2,015	886	1,938	18	16

There are no provisions in respect of any failure, or anticipated failure, to repay any of the above loans or interest thereon. There is no interest, which, having fallen due on the above loans has not been paid.

There are no guarantees or security entered into by the Group in favour of any of its Directors and no guarantees have been entered into in favour of the Group by its Directors.

2012 Key management personnel	(5) Balance as at 1 January 2012 £'000	(1) (4) Balance as at 31 December 2012 £'000	(2) (3) Aggregate maximum amounts outstanding during the year ended 31 December 2012 £'000	Total number KMP as at 1 January 2012	Total number of KMP as at 31 December 2012
Loans	962	488	868	10	9
Deposits	2,600	2,015	6,768	12	18

Basel II Pillar III disclosures for the Group also include information on remuneration. This can be found on the website of the Bank of Ireland Group.

[1] Balance includes principal and interest.
[2] These figures include credit card exposures at the maximum statement balance. In all cases, key management personnel have not exceeded their approved limits. The maximum approved credit limit on any credit card held by key management personnel is £10,000.
[3] The maximum amount outstanding was calculated using the maximum balance on each account. The highest maximum outstanding liability, during the year ended 31 December 2013, for any member of key management personnel and their close family did not exceed £458,000 (31 December 2012: £694,000). The closing balance includes interest accrued and interest paid; the maximum balance includes interest paid.
[4] Foreign currency amounts are converted to GBP, using exchange rates at 31 December 2013, 31 December 2012 and the average exchange rate for the year, as appropriate.
[5] The opening balance includes balances and transactions with KMP who retired during the previous year and are not therefore related parties during the year.

33 Related party transactions (continued)

(e) Compensation of key management personnel	**Year ended 31 December 2013 £'000**	Year ended 31 December 2012 £'000
Remuneration		
Salaries and other short term benefits	2,459	1,971
Pension benefits	224	186
Total	**2,683**	**2,157**

- Total compensation paid to KMP was £2.7 million for the year ended 31 December 2013 and of this amount £1.3 million was paid to Directors. This compared to £2.2 million and £1.3 million respectively for the comparative year ended 31 December 2012;
- During the year ended 31 December 2013 or the year ended 31 December 2012, there was no remuneration paid to the Executive Directors of the Parent in respect of their services as Non-Executive Directors of the Group, or for managing the Group or its subsidiaries;
- The highest total amount paid to any Director for the year ended 31 December 2013 was £356,621, comprising salary and other benefits (year ended 31 December 2012 was £331,000);
- Two Executive Directors are accruing retirement benefits under Defined Benefit Pension Scheme for year ended 31 December 2013 (three Executive Directors for year ended 31 December 2012);
- Pension costs were paid by the Parent and the costs incurred recharged on an agreed basis through the service level agreements; and
- There were no additional benefits, paid by the Group or any other party, in respect of compensation to the Directors for their services for managing the Group or its subsidiaries, either for the year ended 31 December 2013 or the year ended 31 December 2012.

34 Offsetting financial assets and liabilities

The following tables set out the effect or potential effect of netting arrangements on the Group's financial position. This includes the effect or potential effect of rights of set-off associated with the Group's recognised financial assets and recognised financial liabilities that are subject to an enforceable master netting arrangement, irrespective of whether they are set off in accordance with paragraph 42 of IAS 32.

31 December 2013 **Assets**	**Gross amounts of recognised financial assets £m**	**Gross amounts of recognised financial liabilities[1] set off in the balance sheet £m**	**Net amounts of financial assets presented in the balance sheet £m**
Loans and advances to customers	1,163	(1,163)	-

31 December 2012 Assets	Gross amounts of recognised financial assets £m	Gross amounts of recognised financial liabilities[1] set off in the balance sheet £m	Net amounts of financial assets presented in the balance sheet £m
Loans and advances to customers	1,163	(1,163)	-

[1] *Loans and advances to customers represent loan agreements entered into by the Group that are fully collateralised by the Parent. Ultimate recourse is to the Parent. These loans are netted on the balance sheet against deposits received from the Parent.*

35 Principal undertakings

The Group has holdings in the following entities

Names	Principal Activity	Country of Incorporation	Statutory Year End	Percentage of Ordinary Share Capital held %
NIIB Group Limited	Personal finance and leasing	Northern Ireland	31 December	100
Bank of Ireland Trustee Company Limited	Client Investment Services	Northern Ireland	31 December	100
Midasgrange Limited t/a Post Office Financial Services (POFS)	Retail Financial Services	England and Wales	30 September	100
First Rate Exchange Services Holdings Limited[1]	Foreign Exchange	England and Wales	31 March	50

Copies of the financial statements of the principal undertakings can be obtained from the relevant addresses listed on page 162.

[1] *This entity is a joint venture with the UK Post Office in which the Group holds 50% of the equity of the business.*

36 Other subsidiaries

The Group has a subsidiary, where it does not own more than half of the voting power in the company but which is consolidated.

Activity	Company	31 December 2013 Loan assets £m	31 December 2013 Notes in issue £m	31 December 2012 Loan assets £m	31 December 2012 Notes in issue £m
Acquiring mortgage loans and issuing mortgage backed securities	Bowbell No 1 plc	5,481	3,485	6,197	4,172

The assets of Bowbell No 1 plc (Bowbell) are consolidated in the Group's financial statements and are collateral for its obligations. The creditors of Bowbell have no recourse to the Group.

The Group holds all notes issued by Bowbell and none of its assets was pledged by the Group as collateral, for liabilities or contingent liabilities, at 31 December 2013 or at 31 December 2012.

The ultimate holding company of Bowbell, owning 100% of its ordinary share capital and voting rights, is Bowbell No 1 Holdings Limited. Bowbell No 1 plc was incorporated in Great Britain.

37 Common control transactions

Year ended 31 December 2013

There were no common control transactions during the year ended 31 December 2013.

Year ended 31 December 2012

The following transaction occurred:

NIIB Group Limited

In January 2012 the Group agreed with BoI UK Holdings plc to purchase NIIB Group Limited. As this was the transfer of a business between two parties under common control, the Group accounted for this transaction using predecessor accounting as per its accounting policy.

BoI UK Holdings plc transferred the assets and liabilities set out below to the Group. These were initially measured by the Group at their existing carrying value in the consolidated financial statements of BoI UK Holdings plc Group, as prepared under IFRS.

On the date of transfer, the Group paid cash consideration of £7.7 million. Net cash and cash equivalents transferred to the Group of £25 million are reported as cash acquired from common control in investing activities in the cash flow statement on page 67 and 68.

Consolidated balance sheet	18 January 2012 £m
Assets	
Loans and advances to banks	25
Loans and advances to customers	834
Deferred tax assets	4
Other assets	3
Total assets	**866**
Equity and liabilities	
Deposits from banks	823
Customer accounts	4
Other liabilities	8
Provisions	1
Retirement benefit obligation	2
Current tax liability	18
Total liabilities	**856**
Equity	
Share capital	8
Retained earnings	2
Total equity	**10**
Total equity and liabilities	**866**
Included in the above figures:	
Loans and advances to banks - amounts due from the Parent	24
Deposits from banks - amounts due to the Parent	823
Customer accounts - amounts due from entities controlled by the Parent	4

Included within the assets and liabilities presented above were:

- a provision amount of £17 million within loans and advances to customers; and
- retirement benefit obligation presented gross as £18.8 million as the market value of scheme assets, offset by £20.6 million as the present value of the scheme obligations leaving a net pension scheme deficit of £2 million.

37 Common control transactions (continued)

Notes in Circulation

In May 2012, under the Bank of Ireland (UK) plc Act 2012, the authority to issue banknotes and the liability for existing banknotes issued by the Parent in Northern Ireland, transferred from Bank of Ireland Group to Bank of Ireland (UK) plc. On this date the Parent then transferred the full business relating to notes in circulation to the Group. As this was the transfer of a business between two parties under common control, the Group accounted for this transaction using predecessor accounting as per its accounting policy.

On this date BoI Group transferred the assets and liabilities set out below to the Group.

On that date cash consideration of £44 million was paid by the Group. Net cash and cash equivalents transferred to the Group of £753 million are reported as cash acquired from common control in investing activities in the cash flow statement on page 67 and 68.

	15 May 2012 £m
Assets	
Loans and advances to banks	797
Total Assets	**797**
Other liabilities	
Notes in circulation	753
Total liabilities	**753**
Cash paid	**44**

38 Post balance sheet events

In January 2014 the Group repaid the borrowings of £250 million which had previously been drawn down via the BOE Funding for Lending Scheme.

In February 2014 the Group received PRA approval to purchase a further tranche of mortgages from the Parent, which is currently scheduled to take place in March 2014.

39 Approval of financial statements

The Board of Directors approved the financial statements on 5 March 2014.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:35 Page 133

Bank Financial Statements and Notes

Index

	Page
Independent Auditors' Report	134
Bank Income Statement	135
Bank Statement of Other Comprehensive Income	135
Bank Balance Sheet	136
Bank Statement of Changes in Equity	137
Bank Cash Flow Statement	138

Notes

a	Accounting policies	139
b	Auditors' remuneration	139
c	Cash and cash equivalents	140
d	Derivative financial instruments	140
e	Loans and advances to banks	142
f	Available for sale financial assets	143
g	Loans and advances to customers	143
h	Impairment provisions	144
i	Investment in subsidiaries	145
j	Intangible assets	145
k	Other assets	146
l	Credit risk exposures	147
m	Deposits from banks	150
n	Customer account	150
o	Other liabilities	151
p	Provisions	151
q	Deferred tax	152
r	Subordinated liabilities	152
s	Contingent liabilities and commitments	153
t	Share capital	153
u	Liquidity risk	154
v	Measurement basis of financial assets and financial liabilities	155
w	Transferred financial assets	156
x	Fair values of financial assets and financial liabilities	157
y	Related party transactions	159
z	Common control transactions	161
aa	Post balance sheet events	161
ab	Approval of financial statements	161

Independent Auditors' Report

We have audited the separate Bank financial statements of Bank of Ireland (UK) plc for the year ended 31 December 2013 which comprise the Income Statement, the Statement of other Comprehensive Income, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective responsibilities of directors and auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 62, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Bank's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come, save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Bank's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the Bank's financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2013 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and Report of the Directors for the financial year for which the Parent company financial statements are prepared is consistent with the Bank's financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the Bank, or returns adequate for our audit have not been received from branches not visited by us; or
- the Bank's financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Other matter

We have reported separately on the Group financial statements of Bank of Ireland (UK) plc for the year ended 31 December 2013, which can be found on page 63 of the consolidated financial statements.

Hamish Anderson (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
5 March 2014

Bank Financial Statements and Notes

Bank Income Statement
for the year ended 31 December 2013

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Interest income	1,063	1,239
Interest expense	(686)	(1,003)
Net interest income	**377**	**236**
Fee and commission income	116	110
Fee and commission expense	(111)	(105)
Net trading income	-	2
Other operating income	35	39
Total operating income	**417**	**282**
Operating expenses	(265)	(230)
Operating profit before impairment charges on financial assets	**152**	**52**
Impairment charges on financial assets	(125)	(181)
Profit / (loss) before taxation	**27**	**(129)**
Taxation credit	11	38
Profit / (loss) for the year	**38**	**(91)**

Bank Statement of Other Comprehensive Income
for the year ended 31 December 2013

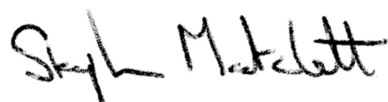
	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Profit / (loss) for the year	**38**	**(91)**
Items that may be reclassified to profit or loss in subsequent periods		
Net change in available for sale reserve (net of tax)[1]	(4)	-
Total comprehensive income / (expense) for the year, net of tax	**34**	**(91)**

[1] *Net of tax of £1 million.*

Bank Balance Sheet
as at 31 December 2013

	Notes	31 December 2013 £m	31 December 2012 £m
Assets			
Cash and cash equivalents	c	4,125	6,380
Items in the course of collection from other banks		182	193
Derivative financial instruments	d	11	10
Loans and advances to banks	e	12,635	26,871
Available for sale financial assets	f	482	341
Loans and advances to customers	g	18,078	18,197
Investment in subsidiaries	i	9	74
Interest in jointly controlled entity		2	2
Intangible assets	j	46	52
Current tax asset		12	-
Other assets	k	103	128
Deferred tax asset	q	117	65
Total assets		**35,802**	**52,313**
Equity and liabilities			
Deposits from banks	m	11,638	25,705
Customer accounts	n	20,879	23,361
Items in the course of transmission to other banks		94	172
Derivative financial instruments	d	11	9
Other liabilities	o	1,053	1,097
Provisions	p	24	21
Subordinated liabilities	r	658	658
Total liabilities		**34,357**	**51,023**
Equity			
Share capital	t	1,151	1,116
Retained earnings		(89)	(127)
Other reserves		383	301
Total equity		**1,445**	**1,290**
Total equity and liabilities		**35,802**	**52,313**

The financial statements on pages 135 to 161 were approved by the Board on 5 March 2014 and were signed on its behalf by:



Stephen Matchett
Director
5 March 2014
Company Number: 07022885

Bank Statement of Changes in Equity for the year ended 31 December 2013

	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Share capital		
At 1 January	1,116	1,056
Issue of share capital – ordinary	35	60
At 31 December	**1,151**	**1,116**
Retained earnings		
Balance at 1 January	(127)	(6)
Profit / (loss) for the year	38	(91)
Transfer of trade (note 'z')	-	(30)
Balance at 31 December	**(89)**	**(127)**
Other Reserves:		
Available for sale reserve		
Balance 1 January	1	1
Changes in fair value	(5)	-
Deferred tax on reserve movements	1	-
Balance at 31 December	**(3)**	**1**
Capital contribution		
Balance at 1 January	**300**	**300**
Contribution during period	86	-
Balance at 31 December	**386**	**300**
Total other reserves	**383**	**301**
Total shareholders' equity	**1,445**	**1,290**

Included in the above:		
Total comprehensive income / (expense) for the year	34	(91)

Bank Cash Flow Statement
for the year ended 31 December 2013

	Notes	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
Cash flows from operating activities			
Profit / (loss) before taxation		27	(129)
Interest expense on subordinated liabilities and other capital instruments		52	45
Depreciation and amortisation	f, j	9	2
Impairment charge on loans and advances to customers	h	125	181
Net change in prepayments and interest receivable	k	17	34
Net change in accruals and interest payable	o	(102)	28
Dividend income		(34)	(40)
Charge for provisions	p	17	21
Cash flows from operating activities before changes in operating assets and liabilities		**111**	**142**
Net change in items in the course of collection		(67)	17
Net change in derivative financial instruments	d	1	(1)
Net change in loans and advances to banks	c, e	1,284	299
Net change in loans and advances to customers	g	(6)	(3,701)
Net change in other assets	k	8	29
Net change in deposits from banks	m	(14,067)	3,038
Net change in customer accounts	n	(2,482)	2,072
Net change in other liabilities	o	58	(23)
Net change in provisions	p	(14)	-
Net cash flow from operating assets and liabilities		**(15,285)**	**1,730**
Net cash flow from operating activities before taxation		**(15,174)**	**1,872**
Taxation refunded / (paid)		34	(6)
Net cash flow from operating activities		**(15,140)**	**1,866**
Investing activities (section a - see below)		(50)	1,995
Financing activities (section b - see below)		(17)	150
Net change in cash and cash equivalents		**(15,207)**	**4,011**
Opening cash and cash equivalents		20,936	16,925
Closing cash and cash equivalents	c	**5,729**	**20,936**
(a) Investing activities			
Additions to available for sale financial assets	f	(167)	(360)
Redemptions of available for sale financial assets	f	19	280
Disposals of available for sale financial assets	f	-	1,282
Dividend received from jointly controlled entity and subsidiaries		34	40
Additions to intangible assets	j	(3)	(1)
Disposal of intangible assets	j	2	1
Change in investment in subsidiaries	i	65	(25)
Net cash and cash equivalents acquired from common control transfers		-	778
Cash flows from investing activities		**(50)**	**1,995**
(b) Financing activities			
Issue of share capital	t	35	60
Interest paid on subordinated liabilities		(52)	(45)
Issue of subordinated liabilities	r	-	135
Cash flows from financing activities		**(17)**	**150**

Notes to the Bank Financial Statements

a Accounting policies

The Bank financial statements comprise the income statement, the statement of other comprehensive income, the balance sheet, the statement of changes in equity, the cash flow statement, accounting policies and the notes to the Bank financial statements.

The financial statements have been prepared on the going concern basis, in accordance with International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRIC) interpretations, as adopted for use in the European Union and as applied in accordance with the provisions of the Companies Act 2006.

The financial statements have been prepared under the historical cost convention, as modified to include the fair valuation of certain financial instruments. They have been prepared to allow the reader to assess the performance and position of the standalone bank.

The financial statements reflect the financial position of the Bank only and do not consolidate the results of any subsidiaries.

The accounting policies of the Bank are the same as those of the Group which are set out in the Group accounting policies section on pages 70 to 89, where applicable.

The Bank's investment in subsidiaries is stated at cost less impairment.

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting year. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. A description of the critical estimates and judgements is set out on pages 88 and 89 within the accounting policies section.

b Auditors' remuneration

Auditors' remuneration	**Year ended 31 December 2013 £000's**	Year ended 31 December 2012 £000's
Fees payable for the audit of the Bank and Group financial statements	441	474
Audit related assurances services	65	36
Auditors' remuneration	**506**	**510**

The Bank's Audit Committee has reviewed the level of fees and is satisfied that it has not affected the independence of the auditors. Audit related assurances services consist of fees in connection with accounting matters. It is the Bank's policy to subject all major assignments to a competitive tender process.

c Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprises of the following balances:

	31 December 2013 £m	31 December 2012 £m
Cash	37	30
Balances at Central Banks	4,088	6,350
Total cash balances applicable	**4,125**	**6,380**
Loans and advances to banks	12,635	26,871
Less: amounts with a maturity of three months or more	(11,031)	(12,315)
Total loans and advances to banks applicable	**1,604**	**14,556**
Total cash and cash equivalents	**5,729**	**20,936**
Due from the Parent	607	13,545

d Derivative financial instruments

The notional amounts and fair values of derivative instruments held by the Bank are set out in the tables below. Further information on derivatives is outlined in note 13 of the consolidated financial statements.

31 December 2013	**Contract / notional amount £m**	**Fair Value Assets £m**	**Fair Value Liabilities £m**
Derivatives held for trading			
Foreign exchange derivatives	460	7	4
Foreign exchange derivatives – with the Parent	461	4	7
Total derivative assets / liabilities held for trading	**921**	**11**	**11**
Derivatives held as fair value hedges			
Interest rate swaps - with the Parent	381	-	-
Derivatives held as cash flow hedges			
Interest rate swaps - with the Parent	864	-	-
Total derivative assets / liabilities held for hedging	**1,245**	**-**	**-**
Total derivative assets / liabilities	**2,166**	**11**	**11**

31 December 2012	Contract / notional amount £m	Fair Value Assets £m	Fair Value Liabilities £m
Derivatives held for trading			
Foreign exchange derivatives	531	6	3
Equity index linked contracts held	7	1	-
Foreign exchange derivatives – with the Parent	531	3	6
Total derivative assets / liabilities held for trading	1,069	10	9

d Derivative financial instruments (continued)

The years in which the hedged cash flows are expected to occur are shown in the tables below:

31 December 2013	Up to 1 year £m	Up to 2 year £m	2 to 5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	2	1	8	6	17
Forecast payable cash flows	-	-	-	-	-

The hedged cash flows are expected to impact on the income statement in the following years:

31 December 2013	Up to 1 year £m	Up to 2 year £m	2 to 5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	2	2	8	5	17
Forecast payable cash flows	-	-	-	-	-

During the year ended 31 December 2013, there were no forecast transactions to which the Bank has applied hedge accounting which were no longer expected to occur.

e Loans and advances to banks

	31 December 2013 £m	31 December 2012 £m
Placements with other banks	11,653	25,990
Mandatory deposit with Central Banks	982	881
Loans and advances to banks	**12,635**	**26,871**
Amounts include:		
Due from the Parent	11,637	25,860

Represented in placements with other banks are:

- an amount of £11,637 million (31 December 2012: £25,860 million) arising from transactions with the Parent, which primarily relates to the management of the Bank's interest rate risk position. Amounts due to the Parent of £11,629 million (31 December 2012: £25,699 million) are also disclosed in note 'm'. From a counterparty credit risk perspective, whilst these two amounts are disclosed on a gross basis, the Bank has in place a contractual Master Netting Agreement with the Parent, whereby, in the event of default of either party, all amounts due or payable will be settled immediately on a net basis; and
- included within amounts due from the Parent are £337 million of loans, whose return is dependent on movements in various external indices (31 December 2012: £374 million). These loans are designated at fair value through profit or loss. Refer to note 'v'.

During the year ended 31 December 2013, £12.3 billion of balances were repaid by the Bank. For further details, refer to note 33 in the consolidated financial statements.

Represented in mandatory deposits with Central Banks are:

- an amount of £946 million relating to collateral with Bank of England in respect of notes in circulation (31 December 2012: £858 million). £518 million of this refers to non interest bearing collateral; and
- an amount of £36 million in relation to mandatory cash ratio deposits, which are non-interest bearing deposits placed with the Bank of England under the provisions of the Bank of England Act 1998. (31 December 2012: £23 million).

f Available for sale financial assets

	31 December 2013 £m	31 December 2012 £m
Government bonds	143	146
Debt securities listed	338	194
Equity securities listed	1	1
Available for sale financial assets	**482**	**341**

At 31 December 2013 and at 31 December 2012, no available for sale financial assets were pledged in sale and repurchase agreements.

The movements on available for sale financial assets are analysed as follows:	Year ended 31 December 2013 £m	Year ended 31 December 2012 £m
At 1 January	341	1,543
Revaluation, exchange and other adjustments	(5)	1
Additions	167	360
Disposals	-	(1,282)
Redemptions	(19)	(280)
Amortisation	(2)	(1)
Impairment charge	-	-
At 31 December	**482**	**341**

g Loans and advances to customers

	31 December 2013 £m	31 December 2012 £m
Residential mortgages	13,087	12,584
Non-property SME and corporate	2,871	2,820
Property and construction	2,455	3,075
Consumer	372	399
Gross loans and advances to customers	**18,785**	**18,878**
Less: allowance for impairment charges on loans and advances to customers (note 'h')	(707)	(681)
Loans and advances to customers	**18,078**	**18,197**
Amounts include:		
Due from subsidiaries	1,055	1,004
Due from entities controlled by the Parent	7	4

The movement in loans and advances to customers reflects:

- decreases in the commercial lending portfolio of £0.6 billion, primarily reflecting GB Business Banking deleveraging; offset by
- a net increase in residential mortgages arising from the acquisition of a number of mortgage portfolios from the Parent with a total loan value of £1.46 billion for consideration of £1.31 billion (representing a weighted average price of 90%). Included within the discount were both expected credit losses and the differential between the customer interest rates on the assets and current market interest rates for similar assets; and
- excluding mortgage acquisitions, other mortgage lending fell by £0.8 billion, representing £0.9 billion of new loans through the Post Office and NI brands which were more than offset by repayments on the overall mortgage portfolio.

Loans and advances to customers include a portion of mortgages which were pledged under the BOE Funding for Lending Scheme.

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:36 Page 144

h Impairment provisions

The following shows the movement in the impairment provisions during the year ended 31 December 2013 and 31 December 2012:

2013	**Residential mortgages £m**	**Non property SME and corporate £m**	**Property and construction £m**	**Consumer £m**	**Total impairment provisions £m**
Provision at 1 January 2013	44	102	511	24	681
Transfer between provisions	-	17	(17)	-	-
Exchange adjustments	-	-	2	-	2
Provisions utilised	(7)	(28)	(69)	(19)	(123)
Recoveries	-	-	1	4	5
Other movements	(3)	4	16	1	18
Charge to the income statement	7	34	69	14	124
Provision at 31 December 2013	**41**	**129**	**513**	**24**	**707**

2012	Residential mortgages £m	Non property SME and corporate £m	Property and construction £m	Consumer £m	Total impairment provisions £m
Provision at 1 January 2012	33	56	479	26	594
Transfer between provisions	-	35	(35)	-	-
Exchange adjustments	-	-	(2)	-	(2)
Provisions utilised	(8)	(20)	(66)	(24)	(118)
Recoveries	-	-	1	3	4
Other movements	1	3	12	2	18
Charge to the income statement	18	28	122	17	185
Provision at 31 December 2012	44	102	511	24	681

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:36 Page 145

i Investment in subsidiaries

Interest in principal undertakings	31 December 2013 £m	31 December 2012 £m
At 1 January	74	101
Increase in investments	-	25
Repayment of investment	(65)	-
Transfer of trade from Midasgrange	-	(52)
At 31 December	**9**	**74**

Repayment of capital

In the year ended 31 December 2013 the Bank received a repayment of capital of £65 million from Midasgrange.

Impairment review

The Group's investments in subsidiaries are reviewed if events or circumstances indicate that impairment may have occurred by comparing the carrying value of each investment to its recoverable amount. An impairment charge arises if the carrying value exceeds the recoverable amount. No impairment was identified in the year ended 31 December 2013 or the year ended 31 December 2012.

Increase in investments - Year ended 31 December 2012

The Bank purchased 100% of the total share capital of NIIB Group Ltd for consideration of £8 million in January 2012. Refer to note 37 to the consolidated financial statements for further details.

The Bank had also invested an additional £11 million in Midasgrange Ltd in March 2012 before the purchase of the non controlling interest in August 2012 resulting in a further £6 million increase in investment.

Transfer of trade - Year ended 31 December 2012

On 3 September 2012 the business and trade of Midasgrange Ltd was transferred into the Bank. As a consequence the value of the investment of £118 million was reduced accordingly, to the value of the net assets of £66 million acquired through equity, resulting in a move of £47 million. Refer to note 'z' for further details.

j Intangible assets

2013	Computer software externally purchased £m	Other computer software internally generated £m	Externally purchased intangible assets £m	Total £m
Cost				
At 1 January 2013	7	34	73	114
Additions	1	-	2	3
Disposals / write-offs	(8)	-	-	(8)
At 31 December 2013	**-**	**34**	**75**	**109**
Accumulated amortisation				
At 1 January 2013	(5)	(23)	(34)	(62)
Disposals / write down	6	-	-	6
Charge to the income statement	(1)	(3)	(3)	(7)
At 31 December 2013	**-**	**(26)**	**(37)**	**(63)**
Net book value at 31 December 2013	**-**	**8**	**38**	**46**

j Intangible assets (continued)

2012	Computer software externally purchased £m	Other computer software internally generated £m	Externally purchased intangible assets £m	Total £m
Cost				
At 1 January 2012	-	-	-	-
Transfers from Group undertakings	8	34	71	113
Additions	-	-	1	1
Disposals / write-offs / other movements	(1)	-	1	-
At 31 December 2012	7	34	73	114
Accumulated amortisation				
At 1 January 2012	-	-	-	-
Transfers from Group undertakings	(5)	(22)	(33)	(60)
Charge to the income statement	-	(1)	(1)	(2)
At 31 December 2012	(5)	(23)	(34)	(62)
Net book value at 31 December 2012	2	11	39	52

Refer to note 19 in the Consolidated Financial Statements for further details.

k Other assets

	31 December 2013 £m	31 December 2012 £m
Sundry and other receivables	16	24
Interest receivable	43	62
Accounts receivable and prepayments	44	42
Other assets	**103**	**128**
Amounts include:		
Due from the Parent	33	59
Maturity profile of other assets		
Receivable within 1 year	64	95
Receivable after 1 year	39	33

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:36 Page 147

I Credit risk exposures

The following tables represent the credit risk exposures of the Bank for its loans and advances to customers and other financial instruments. The Group exposures can be found in Risk management section 2.1.

Asset Quality - Loans and advances to customers

The table and analysis below summarise the Bank's loans and advances to customers by risk profile (before impairment provisions).

31 December 2013	Residential mortgages £m	Non-property SME and corporate £m	Property and construction £m	Consumer £m	Total loans and advances to customers £m	Total loans and advances to customers %
High quality	12,436	425	78	331	13,270	71%
Satisfactory quality	21	1,890	605	-	2,516	14%
Acceptable quality	49	128	282	-	459	2%
Lower quality but not past due nor impaired	-	118	320	-	438	2%
Neither past due nor impaired	**12,506**	**2,561**	**1,285**	**331**	**16,683**	**89%**
Past due but not impaired	504	17	109	19	649	3%
Impaired	77	293	1,061	22	1,453	8%
Total	**13,087**	**2,871**	**2,455**	**372**	**18,785**	**100%**

31 December 2012	Residential mortgages £m	Non-property SME and corporate £m	Property and construction £m	Consumer £m	Total loans and advances to customers £m	Total loans and advances to customers %
High quality	11,997	372	91	356	12,816	68%
Satisfactory quality	146	1,874	966	-	2,986	16%
Acceptable quality	-	158	451	-	609	3%
Lower quality but not past due nor impaired	-	140	267	-	407	2%
Neither past due nor impaired	12,143	2,544	1,775	356	16,818	89%
Past due but not impaired	375	28	113	21	537	3%
Impaired	66	248	1,187	22	1,523	8%
Total	12,584	2,820	3,075	399	18,878	100%

At 31 December 2013 included within the non-property SME and corporate book is £1,061 million (31 December 2012: £1,008 million) in relation to intra-group funding balances with the Bank's subsidiaries with no banking license, the largest balance being £876 million (31 December 2012: £811 million) relating to NIIB. All of these balances were classified within satisfactory quality.

I Credit risk exposures (continued)

Financial Assets - 'past due but not impaired': Loans and advances to customers

The tables below provide an analysis of loans and advances to customers ' past due but not impaired' by asset classification

31 December 2013	**Residential mortgages £m**	**Non-property SME and corporate £m**	**Property and construction £m**	**Consumer £m**	**Total £m**
Past due up to 30 days	101	9	29	10	149
Past due 31-60 days	240	6	44	5	295
Past due 61-90 days	64	2	36	4	106
Past due more than 90 days	99	-	-	-	99
Total	**504**	**17**	**109**	**19**	**649**

31 December 2012	Residential mortgages £m	Non-property SME and corporate £m	Property and construction £m	Consumer £m	Total £m
Past due up to 30 days	67	11	10	12	100
Past due 31-60 days	173	10	77	5	265
Past due 61-90 days	56	7	26	4	93
Past due more than 90 days	79	-	-	-	79
Total	375	28	113	21	537

Financial Assets - 'Impaired': Loans and advances to customers

The table below provides an analysis of impaired loans and advances to customers by composition

31 December 2013	**Advances £m**	**Impaired loans £m**	**Impaired loans as % of advances £m**	**Impairment provisions £m**	**Impairment provisions as % of impaired loans £m**
Residential mortgages	13,087	77	1%	41	53%
Non-property SME and corporate	2,871	293	10%	129	44%
Property and construction	2,455	1,061	43%	513	48%
Consumer	372	22	6%	24	109%
Total	**18,785**	**1,453**	**8%**	**707**	**49%**

31 December 2012	Advances £m	Impaired loans £m	Impaired loans as % of advances £m	Impairment provisions £m	Impairment provisions as % of impaired loans £m
Residential mortgages	12,584	66	1%	43	65%
Non-property SME and corporate	2,820	248	9%	102	41%
Property and construction	3,075	1,187	39%	512	43%
Consumer	399	22	6%	24	109%
Total	18,878	1,523	8%	681	45%

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:36 Page 149

I Credit risk exposures (continued)

Impairment provision

The tables below split out the impairment provisions by its nature and composition

	31 December 2013 £m	31 December 2012 £m
Specific provisions	627	603
Incurred but not reported (IBNR)	80	78
Total impairment provision	**707**	**681**

	31 December 2013			31 December 2012		
	Specific £m	**IBNR £m**	**Total £m**	Specific £m	IBNR £m	Total £m
Residential mortgages	5	3	8	9	5	14
Non-property SME and corporate	34	-	34	26	2	28
Property and construction	69	-	69	132	(10)	122
Consumer	14	-	14	16	1	17
Total loan impairment charge / (release)	**122**	**3**	**125**	**183**	**(2)**	**181**

Asset quality: other financial instruments

Other financial instruments include available for sale assets, derivative financial instruments and loans and advances to banks.

Other financial instruments with ratings equivalent to:	**31 December 2013 £m**	31 December 2012 £m
AAA to AA-	1,464	1,222
A+ to A-	23	137
BBB+ to BB-	11,641	25,863
Total	**13,128**	**27,222**

Refer to the Risk management section for details on residential and commercial forbearance and repossessed collateral on pages 39 to 42.

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

m Deposits from banks

	31 December 2013 £m	31 December 2012 £m
Deposits from banks	11,638	25,705
Deposits from banks	**11,638**	**25,705**
Amounts include:		
Due to the Parent	**11,629**	**25,699**

Amounts due to the Parent of £11,629 million (31 December 2012: £25,699 million) relates to borrowing in place to fund and manage interest rate risk on the Bank's assets. Refer to note 'e' for details of amounts due from the Parent, and note 33 of the consolidated financial statements in respect of changes in these balances during 2013.

n Customer accounts

	31 December 2013 £m	31 December 2012 £m
Term deposits	10,005	12,450
Demand deposits	8,331	8,501
Interest bearing current accounts	785	989
Non interest bearing current accounts	1,758	1,421
Customer accounts	**20,879**	**23,361**
Amounts include:		
Due to subsidiaries	22	86
Due to entities controlled by the Parent	18	114

Term deposits include deposits of £337 million (31 December 2012: £374 million), whose return is dependent on movements in various external indices; these deposits are designated at fair value through profit or loss. Refer to note 'v' for details on fair value.

o Other liabilities

	31 December 2013 £m	31 December 2012 £m
Accrued interest payable	133	227
Notes in circulation	826	759
Sundry payables	83	92
Accruals and deferred income	11	19
Other liabilities	**1,053**	**1,097**
Amounts include:		
Due to the Parent	24	33
Maturity profile of other liabilities		
Amounts payable within 1 year	1,052	1,092
Amounts payable after 1 year	1	5

The Parent was previously authorised to issue banknotes in Northern Ireland under the Banking Act 2009. From 15 May 2012, under the Bank of Ireland (UK) plc Act 2012, that authority to issue banknotes and the liability for existing banknotes issued by the Parent in Northern Ireland transferred to the Bank. Refer to note 37 in the consolidated financial statements for further details.

p Provisions

	31 December 2013			31 December 2012		
	Payment protection insurance £m	**Financial services compensation scheme £m**	**Total £m**	Payment protection insurance £m	Financial services compensation scheme £m	Total £m
At 1 January	2	19	21	1	-	1
Charge to the income statement	-	17	17	2	19	21
Utilised during the year	(1)	(13)	(14)	(1)	-	(1)
At 31 December	**1**	**23**	**24**	**2**	**19**	**21**
Expected utilisation period						
Used within 1 year	1	15	16	1	13	14
Used after 1 year	-	8	8	1	6	7

Payment protection insurance (PPI)

As at 31 December 2013 the Bank is holding a provision of £1 million (year ended 31 December 2012: £2 million) to cover potential customer claims for refunds of premiums associated with the alleged mis-selling of PPI policies. The provision is based upon known pipeline cases and the expectation of future claims. The closing provision represents managements' best estimate of expected costs.

Financial services compensation scheme (FSCS)

The FSCS is the UK's independent statutory compensation fund for customers of authorised financial services firms and pays compensation if a firm is unable to pay claims against it. The FSCS is funded by levies on the industry. Following the default of a number of financial institutions, the FSCS borrowed funds from HM Treasury to cover compensation in relation to protected deposits. The FSCS recovers the interest cost and capital repayments, together with on-going management expenses, by way of annual levies on member firms. If the assets of the failed institutions are insufficient to repay the Government loan additional levies may become payable in future periods. The provisions at 31 December 2013 represents the Bank's estimate of levies due for the year ended 31 December 2013 and 31 December 2012, less payments made to date.

Business Review
Risk Management
Governance
Consolidated Financial Statements
Bank Financial Statements
Other Information

q Deferred tax

	31 December 2013 £m	31 December 2012 £m
The movement on the deferred tax account is as follows:		
At 1 January	65	20
Income statement (charge) / credit for year	(35)	38
Losses transferred from Parent	86	-
Available for sale securities - transferred to reserves	1	-
Other movements	-	7
At 31 December	**117**	**65**
Deferred tax assets and liabilities are attributable to the following items:		
Deferred tax assets		
Unutilised tax losses	117	66
Available for sale securities	1	-
Total deferred tax assets	**118**	**66**
Deferred tax liabilities		
Fixed assets	(1)	(1)
Total deferred tax liabilities	**(1)**	**(1)**
Represented on the balance sheet as follows:		
Deferred tax assets	**117**	**65**

Refer to note 26 of the Consolidated Financial Statements for further details.

r Subordinated liabilities

	31 December 2013 £m	31 December 2012 £m
£523 million subordinated floating rate loans 2020	523	523
£90 million subordinated floating rate loans 2022	90	90
£45 million subordinated floating rate loans 2022	45	45
Subordinated liabilities	**658**	**658**

Refer to note 27 of the consolidated financial statements, for further details.

s Contingent liabilities and commitments

The table below gives the contractual amounts of contingent liabilities and commitments. The maximum exposure to credit loss under contingent liabilities and commitments is the contractual amount of the instrument in the event of non-performance by the other party where all counter claims, collateral, or security prove worthless.

	31 December 2013 Contractual amount £m	31 December 2012 Contractual amount £m
Contingent liabilities		
Guarantees and irrevocable letters of credit	15	14
Other contingent liabilities	8	9
Total contingent liabilities	**23**	**23**
Commitments		
Undrawn formal standby facilities, credit lines and other commitments to lend		
- revocable or irrevocable with original maturity of 1 year or less	2,989	3,151
- irrevocable with original maturity of over 1 year	217	232
Total commitments	**3,206**	**3,383**

Refer to note 28 of the consolidated financial statements, for further details.

t Share capital

Movements in ordinary and preference shares	**Ordinary[1] Shares**		Preference[1] Shares	
	31 December 2013 £m	31 December 2012 £m	**31 December 2013 £m**	31 December 2012 £m
At 1 January	816	756	300	300
Issued during the year	35	60	-	-
At end of year	**851**	**816**	**300**	**300**

[1] *All shares issued are in denominations of £1, therefore the table above also represents unit values.*

Refer to note 29 of the consolidated financial statements, for further details.

u Liquidity risk

The tables below summarise the maturity profile of the Bank's financial liabilities at 31 December 2013 and at 31 December 2012, based on contractual undiscounted repayment obligations.

The Bank does not manage liquidity risk on the basis of contractual maturity. Instead, the Bank manages liquidity risk based on expected cash flows. The balances will not agree directly to the balance sheet because the table incorporates all cash flows, on an undiscounted basis, related to both principal and interest payments.

Customer accounts include a number of term accounts that contain easy access features. These allow the customer to access a portion or all of their deposit notwithstanding that this repayment could result on a financial penalty being paid by the customer. For such accounts the portion subject to the potential early access has been classified accordingly in the table below.

As at 31 December 2013	**Demand £m**	**Up to 3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Deposits from banks	623	35	6,328	4,722	151	11,859
Customer accounts	12,353	3,672	3,529	1,397	-	20,951
Subordinated liabilities	-	5	49	245	839	1,138
Contingent liabilities	23	-	-	-	-	23
Commitments	2,989	-	-	217	-	3,206
Total	**15,988**	**3,712**	**9,906**	**6,581**	**990**	**37,177**

As at 31 December 2012	Demand £m	Up to 3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Deposits from banks	1,769	18,992	1,746	3,286	178	25,971
Customer accounts	12,439	10,089	728	208	1	23,465
Subordinated liabilities	-	5	51	217	889	1,162
Contingent liabilities	23	-	-	-	-	23
Commitments	3,151	-	-	232	-	3,383
Total	17,382	29,086	2,525	3,943	1,068	54,004

The table below summarises the maturity profile of the Bank's derivative liabilities. The Bank manages liquidity risk based on expected cash flows, therefore the undiscounted cash flows payable on derivatives liabilities are classified according to their contractual maturity.

31 December 2013	**Demand £m**	**Up to 3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Gross settled derivative liabilities - outflows	-	(318)	(142)	(10)	-	(470)
Gross settled derivative liabilities - inflows	-	311	139	10	-	460
Gross settled derivative liabilities - net flows	-	(7)	(3)	-	-	(10)
Net settled derivative liabilities	-	-	1	1	(3)	(1)
Total derivatives cash flows	**-**	**(7)**	**(2)**	**1**	**(3)**	**(11)**

31 December 2012	Demand £m	Up to 3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Gross settled derivative liabilities - outflows	-	(321)	(195)	(28)	-	(544)
Gross settled derivative liabilities - inflows	-	315	192	28	-	535
Gross settled derivative liabilities - net flows	-	(6)	(3)	-	-	(9)
Net settled derivative liabilities	-	-	-	-	-	-
Total derivatives cash flows	-	(6)	(3)	-	-	(9)

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:36 Page 155

v Measurement basis of financial assets and financial liabilities

The table below analyses the carrying amounts of the financial assets and financial liabilities, by accounting treatment and by balance sheet heading.

	At fair value through profit or loss		At fair value through other comprehensive income (OCI)			
31 December 2013	**Held for trading £m**	**Designated upon initial recognition £m**	**Held for Hedging[1] £m**	**Available for sale £m**	**Held at amortised cost £m**	**Total £m**
Financial assets						
Cash and balances at Central Banks	-	-	-	-	4,125	4,125
Items in course of collection from other banks	-	-	-	-	182	182
Derivative financial instruments	11	-	-	-	-	11
Loans and advances to banks	-	337	-	-	12,298	12,635
Available for sale financial assets	-	-	-	482	-	482
Loans and advances to customers	-	-	-	-	18,078	18,078
Total financial assets	11	337	-	482	34,683	35,513
Financial liabilities						
Deposits by banks	-	-	-	-	11,638	11,638
Customer accounts	-	337	-	-	20,542	20,879
Items in course of transmission to other banks	-	-	-	-	94	94
Derivative financial instruments	11	-	-	-	-	11
Subordinated liabilities	-	-	-	-	658	658
Total financial liabilities	11	337	-	-	32,932	33,280

[1] *The amounts relating to derivatives held for hedging are too small for presentation*

The fair value and contractual amount due on maturity, of financial liabilities designated at fair value upon initial recognition, are shown in the table below.

	31 December 2013		31 December 2012	
	Fair values £m	**Contractual amount due to Maturity £m**	Fair Values £m	Contractual amount due to Maturity £m
Customer accounts	337	333	374	368

v Measurement basis of financial assets and financial liabilities (continued)

31 December 2012	At fair value through profit or loss		At fair value through other comprehensive income (OCI)		
	Held for trading £m	Designated upon initial recognition £m	Available for sale £m	Held at amortised cost £m	Total £m
Financial assets					
Cash and balances at Central Banks	–	-	-	6,380	6,380
Items in course of collection from other banks	-	-	-	193	193
Derivative financial instruments	10	-	-	-	10
Loans and advances to banks	-	374	-	26,497	26,871
Available for sale financial assets		-	341	-	341
Loans and advances to customers	-	-	-	18,197	18,197
Total financial assets	10	374	341	51,267	51,992
Financial liabilities					
Deposits from banks	-	-	-	25,705	25,705
Customer accounts	-	374	-	22,987	23,361
Items in course of transmission to other banks	-	-	-	172	172
Derivative financial instruments	9	-	-	-	9
Subordinated liabilities	-	-	-	658	658
Total financial liabilities	9	374	-	49,522	49,905

w Transferred financial assets

Securitisation	**Carrying amount of assets £m**	**Carrying amount of associated liabilities £m**	**Fair value of transferred assets £m**	**Fair value of associated liabilities (Fair value of notes in issue) £m**
Residential mortgage book (Bowbell)	5,303	5,303	5,033	5,033

Nature of risks and rewards to which the entity is exposed

The Bank is exposed substantially to all risks and rewards including credit and market risk associated with the transferred assets.

The Bowbell mortgage book is ring-fenced whereby the cash flows associated with assets can only be used to repay the Bowbell notes holders plus associated issuance fees or costs.

Entity continuing to recognise assets to the extent of its continuing involvement

The Bank is not recognising any asset to the extent of its continuing involvement.

x Fair value of financial assets and financial liabilities

Fair value hierarchy
Further information on fair value is shown in note 32 of the consolidated financial statements.

Level 1 comprises financial assets and financial liabilities valued using quoted market prices in active markets. An active market is one in which transactions occur with sufficient volume and frequency to provide pricing information on an ongoing basis.

Level 2 comprises financial assets and financial liabilities valued using techniques based significantly on observable market data.

Level 3 comprises financial assets and financial liabilities valued using techniques where the impact of the non-observable market data is significant in determining the fair value of the instrument. Non-observable market data is not readily available in an active market due to market illiquidity or complexity of the product. These inputs are generally determined based on observable inputs of a similar nature, historic observations on the level of the input, or analytical techniques.

31 December 2013	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets held at fair value				
Derivative financial instruments	-	11	-	11
Loans and advances to banks	-	337	-	337
AFS financial assets	481	1	-	482
Total financial assets at fair value	**481**	**349**	**-**	**830**
As a % of fair value assets	**58%**	**42%**	**-**	**100%**
Financial liabilities held at fair value				
Customer accounts	-	337	-	337
Derivative financial instruments	-	11	-	11
Total financial liabilities at fair value	**-**	**348**	**-**	**348**
As a % of fair value liabilities	**-**	**100%**	**-**	**100%**

31 December 2013	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets held at amortised cost				
Cash and balances at central banks	4,125	-	-	4,125
Items in the course of collection from other banks	182	-	-	182
Loans and advances to banks	-	12,420	-	12,420
Loans and advances to customers	-	-	17,459	17,459
Total	**4,307**	**12,420**	**17,459**	**34,186**
Financial liabilities held at amortised cost				
Deposits from banks	-	11,679	-	11,679
Customer accounts	-	20,588	-	20,588
items in the course of transmission to other banks	94	-	-	94
Subordinated liabilities	-	694	-	694
Total	**94**	**32,961**	**-**	**33,055**

The Bank had no assets or liabilities held at fair value on the balance sheet within level 3 at 31 December 2013 or 31 December 2012. There were also no transfers in or out of level 3 during the year ended 31 December 2013 or 31 December 2012.

x Fair value of financial assets and financial liabilities (continued)

31 December 2012	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets held at fair value				
Derivative financial instruments	1	9	-	10
Loans and advances to banks	-	374	-	374
AFS financial assets	341	-	-	341
Total financial assets at fair value	342	383	-	725
As a % of fair value assets	47%	53%	-	100%
Financial liabilities held at fair value				
Customer accounts	-	374	-	374
Derivative financial instruments	-	9	-	9
Total financial liabilities at fair value	-	383	-	383
As a % of fair value liabilities	-	100%	-	100%

The carrying amount and the fair value of the Bank's financial assets and financial liabilities as at 31 December 2013 and 31 December 2012 are set out in the table below:

	31 December 2013		31 December 2012	
	Carrying amount £m	**Fair values £m**	Carrying amount £m	Fair values £m
Financial Assets				
Cash and balances at Central Banks[1]	4,125	4,125	6,380	6,380
Items in course of collection from other banks[1]	182	182	193	193
Loans and advances to banks	12,635	12,757	26,871	27,081
Available for sale financial assets[1]	482	482	341	341
Derivatives financial assets[1]	11	11	10	10
Loans and advances to customers	18,078	17,459	18,197	16,844
Financial Liabilities				
Deposits from banks	11,638	11,679	25,705	25,869
Items in the course of transmission to other banks[1]	94	94	172	172
Derivative financial liabilities[1]	11	11	9	9
Customer accounts	20,879	20,925	23,361	23,505
Subordinated liabilities	658	694	658	666

[1] The fair value of these financial instruments is equal to the carrying value. These instruments are either carried at market value or have minimal credit losses, and are either short term in nature or re-priced frequently.

y Related party transactions

The Bank was incorporated in England and Wales on 17 September 2009 and is a wholly controlled entity of the Governor and Company of the Bank of Ireland (The Parent).

A number of banking transactions are entered into between the Bank, its subsidiaries, joint ventures and the Parent in the normal course of business. These include loans, deposits and foreign currency transactions. The amounts included in the accounts are set out by category in the following tables.

Further information on related parties and key management personnel is shown in note 33 of the consolidated financial statements and a list of the Bank's principal undertakings can be found in note 35 of the consolidated financial statements.

Amounts included in the financial statements at 31 December 2013, in aggregate, by category of related party, are as follows:

31 December 2013	Parent[1] £m	Subsidiaries £m	Jointly controlled entity £m	Total £m
Income statement				
Interest income	315	24	-	339
Interest expense	(262)	-	-	(262)
Fee and commission income	3	-	-	3
Fees and commission expense	(11)	-	-	(11)
Net trading income / (expense)	21	-	-	21
Other operating income	-	-	34	34
Impairment charges on financial assets	(1)	-	-	(1)
Operating expenses paid for services provided[2]	(189)	-	-	(189)
Total income / (expense)	**(124)**	**24**	**34**	**(66)**
Assets:				
Loans and advances to banks	11,637	-	-	11,637
Loans and advances to customers	7	1,055	-	1,062
Other assets	33	-	-	33
Derivatives	4	-	-	4
Total assets	**11,681**	**1,055**	**-**	**12,736**
Liabilities:				
Deposits from banks	11,629	-	-	11,629
Customer accounts	18	22	-	40
Other liabilities	24	-	-	24
Derivatives	7	-	-	7
Total liabilities	**11,678**	**22**	**-**	**11,700**
Net exposure	**3**	**1,033**	**-**	**1,036**

[1] This relates to amounts in respect of the Parent and entities controlled by the Parent.
[2] Included within this amount is a fee of £50,000 (year ended 31 December 2012: £25,000) to Archie Kane, Governor and non-executive Director of the Parent who was appointed as consultant advisor to the Group in June 2012.

y Related party transactions (continued)

31 December 2012	Parent[1] £m	Subsidiaries £m	Jointly controlled entity £m	Total £m
Income statement				
Interest received	617	15	-	632
Interest paid	(503)	12	-	(491)
Fee and commission income	-	1	-	1
Fees and commission expense	(10)	(27)	-	(37)
Trading income / (expense)	(5)	-	-	(5)
Other operating income	-	-	40	40
Impairment charges on financial assets	4	-	-	4
Operating expenses paid for services provided[2]	(174)	-	-	(174)
Total income / (expense)	(71)	1	40	(30)
Assets:				
Loans and advances to banks	25,860	-	-	25,860
Loans and advances to customers	4	1,004	-	1,008
Other assets	59	-	-	59
Derivatives	3	-	-	3
Total assets	25,926	1,004	-	26,930
Liabilities:				
Deposits from banks	25,699	-	-	25,699
Customer accounts	114	86	-	200
Other liabilities	33	-	-	33
Derivatives	6	-	-	6
Total liabilities	25,852	86	-	25,938
Net exposure	74	918	-	992

[1] This relates to amounts in respect of the Parent and entities controlled by the Parent.
[2] Included within this amount is a fee of £25,000 to Archie Kane, Governor and non-executive Director of the Parent who was appointed as consultant advisor to the Group in June 2012.

z Common control transactions

Year ended 31 December 2013
There were no common control transactions during the year ended 31 December 2013.

Year ended 31 December 2012
The following transaction occurred:

Midasgrange transfer of trade in the year ended 31 December 2012
On 3 September 2012 Midasgrange, now a wholly owned subsidiary, transferred its business and trade to the Bank as part of a Group restructure. The net assets transferred at that date comprise of the net assets of Midasgrange £65 million and any assets arising on consolidation; in this case a £21 million intangible asset relating to customer distribution rights.

Settlement of the Midasgrange net assets of £66 million was made through an intercompany liability account in the Bank. Net cash and cash equivalents transferred to the Bank of £25 million were reported as cash acquired in investing activities in the cash flow statement on page 138.

Balance sheet	3 September 2012 £m
Intangible assets – other	54
Deferred tax asset	7
Loans and advances to banks	25
Other assets	42
Total Assets	**128**
Other liabilities	36
Deposits from banks	5
Total liabilities	**41**
Net assets transferred	**87**

Notes in circulation
Details of the amounts acquired as part of the notes in circulation business acquisition can be found in note 37 to the consolidated financial statements.

aa Post balance sheet events

In January 2014 the Group repaid the borrowings of £250 million which had previously been drawn down via the BOE Funding for Lending Scheme.

In February 2014 the Group received PRA approval to purchase a further tranche of mortgages from the Parent, which is currently scheduled to take place in March 2014.

ab Approval of financial statements

The Board of Directors approved the financial statements on 5 March 2014.

Other Information

Principal Business Units and Addresses

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First Rate Exchange Services
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Website: www.firstrate.co.uk
Managing Director: Gordon Gourlay

NIIB Group Limited
1 Donegall Square South, Belfast BT1 5LR
Tel: + 44 844 892 1848

Abbreviations

ACIB	Associate, Chartered Institute of Bankers
AFS	Available for Sale
ALCO	Asset and Liability Committee
ATM	Automatic Teller Machine
BA	Bachelor of Arts
BA (Mod) Econ	Bachelor of Arts (Moderatorship) in Economics
BComm	Bachelor of Commerce
BOE	Bank of England
BoI	Bank of Ireland
bps	Basis points
BRC	Board Risk Committee
BSc	Bachelor of Science
BSc (Econ)	Bachelor of Science in Economics
CCO	Chief Credit Officer
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CML	Council of Mortgage Lenders
CPI	Consumer Price Inflation
CRD	Capital Requirement Directive (EU)
CRO	Chief Risk Officer
CRPC	Credit Risk and Portfolio Committee
CRR	Capital Requirements Regulation
CSA	Credit Support Annex
DCF	Discounted Cash Flow
DipFS	Diploma in Financial Studies
EBA	European Banking Authority
ECB	European Central Bank
e.g.	Exempli gratia (for example)
ELG	Eligible Liabilities Guarantee Scheme
EU	European Union
FCA	Financial Conduct Authority
FCIOBS	Fellow of the Chartered Institute of Bankers
FCMA	Fellow Chartered Management Accountant
FLS	Funding for Lending Scheme
FRES	First Rate Exchange Services Limited
FRESH	First Rate Exchange Services Holdings Limited
FRS	Financial Reporting Standard
FSA	Financial Services Authority
FSCS	Financial Services Compensation Scheme
FTSE	Financial Times Stock Exchange
FVTPL	Fair Value through Profit or Loss
FX	Foreign Exchange
GBP	ISO 4217 currency code for Pound Sterling
GCR	Group Credit Review
GDP	Gross Domestic Product
GRPC	Group Risk Policy Committee
HSBC	Hong Kong & Shanghai Banking Corporation
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IBNR	Incurred but not Reported
ICAAP	Internal Capital Adequacy Assessment Process
i.e.	Id est (that is)
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standards
ILAA	Individual Liquidity Adequacy Assessment
IMF	International Monetary Fund
IPD	Investment Property Databank
ISDA	International Swaps and Derivatives Association
IT	Information Technology
JCE	Jointly Controlled Entity
JCO	Jointly Controlled Operation
KMP	Key Management Personnel
LCR	Liquidity Coverage Ratio
LGD	Loss Given Default
LIBOR	London Interbank Offered Rate
LLB	Legum Baccalaureus (Bachelor of Law)
LLP	Limited Liability Partnership
LTD	Limited
LTV	Loan to Value
MA (Econ)	Master of Economics
MSc	Master of Science
NSFR	Net Stable Funding Ratio
OCI	Other Comprehensive Income
Pari passu	On equal footing
PD	Probability of Default
POFS	Post Office Financial Services
PPI	Payment Protection Insurance
PRA	Prudential Regulation Authority
PwC	PricewaterhouseCoopers LLP
RMBS	Residential Mortgage Backed Securitisation
RORC	Regulatory and Operational Risk Committee
R&ORM	Regulatory and Operational Risk Management
RPI	Retail Price Inflation
RWA	Risk Weighted Assets
SIC	Standing Interpretations Committee
SLA	Service Legal Agreement
SME	Small / Medium Enterprises
SOCI	Statement of Other Comprehensive Income
SPE	Special Purpose Entity
STG	Pound Sterling
£m	Million
£bn	Billion
£'000	Thousands

UK BOI Annual Report 2013_UK BOI Annual Report 19/03/2014 12:37 Page 164

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