Bank of Ireland (UK) plc
Annual Report 2017

Bank of Ireland UK
The Partnership Bank

Bank of Ireland (UK) plc
Annual Report

for the year ended 31 December 2017

Company Number: 07022885

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Contents

Bank of Ireland (UK) plc (the 'Bank'), together with its subsidiary undertakings (which together comprise the 'Group') is the principal United Kingdom retail and commercial banking business of the Governor and Company of the Bank of Ireland (the 'Parent').

Percentages throughout the document are calculated on the absolute underlying figures and so may differ from the percentages calculated on the rounded numbers presented, where the percentages are not measured this is indicated by n/m.

Business Review

Key highlights

During 2017, the Group continued to invest in new products and to extend its distribution reach, with the priority of putting our customers and colleagues at the centre of everything we do. This resulted in a 12% increase in new customer lending at £4.5 billion and an underlying profit before taxation of £151 million.

Profits were lower than the prior year reflecting the increased investment made in the business, changes in the mix and behaviours of our product portfolio, and as a result of the ongoing competition in the UK consumer lending market. We further grew our personal loan and new mortgage business during 2018, significantly reduced our funding costs, acquired a strategically important and complementary car leasing and fleet management business (Marshall Leasing Limited) and continued to win many industry awards.

The UK market offers many opportunities for Bank of Ireland (UK) plc, but inevitably also various challenges. These include continued political and economic uncertainty associated with the outcome of Brexit negotiations, the risk of weakening consumer and business confidence and a highly competitive retail consumer financial services market.

Given this backdrop, we continue to bring the unique Partnership Bank Strategy and its values to life for our customers, colleagues and partners, and strengthening this culture will enable us to deliver our strategic plans for the future.

Looking forward to 2018 I am therefore confident that given the momentum in the business, combined with a strong risk and cost culture and our clear focus on profitable customer and partner offerings, that we will build on our trading performance and deliver sustainable returns for all our stakeholders.

Des Crowley,
Bank of Ireland (UK) plc Chief Executive Officer

Customers

- Continuing to focus on our customers needs and aspirations across all our brands and partners.
- Winning more awards in the year across mortgages, personal lending and foreign exchange products.
- Transforming the customer experience through technical innovation, digitisation and product development.

Profitability

- Profit before tax of £151 million (2016 : £193 million).
- Net interest margin 2.02% (2016 : 2.07%).
- Total operating expenses and change spend of £328 million (2016 : £313 million).
- Impairment charges of £26 million (2016 : £23 million).
- £160 million dividend paid to the Parent (2016 : £220 million).

Capital

- CET1 ratio 14.7%.
- Total capital ratio 20.5%.
- Over £4.5 billion of new customer lending.
- Optimised capital restructure with a net £45 million reduction of Tier 2.
- IFRS 9 transition impact of c.30 bps.

Chairman's statement

2017 has been a year of consolidation with significant investments made to ensure sustained profitability for the Group. We continue to operate in a highly competitive retail consumer financial services market with various uncertainties regarding the possibility of higher interest rates, changes in customer behaviours, and the potential headwinds associated with the UK's decision to leave the European Union.

Against this context I am pleased to report that the Group has built on its significant strengths, including its unique partnership approach to retail banking, introducing new customer propositions and benefitting from a strong capital and funding base. We have invested in our people, systems and customer service and remain focused on delivering compelling and value for money products for the customers we serve. Our strategic priorities are concentrated on:

- Transforming our culture, our technology and our business models;
- Serving our customers brilliantly; and
- Growing sustainable profitability and returns for our shareholders.

2017 financial performance

Our reported underlying profit before tax of £151 million was £42 million lower compared to our 2016 reported profit of £193 million. This year on year performance, reflects a 5% decrease in net interest income (as a result of changes in the mix and behaviours of our product portfolio and the ongoing competition in the UK consumer lending market), offset by improvements in the cost of funding.

In addition we continued to invest for the future, including significant investments in our partnerships, people and propositions, with operating expenses increasing by 5% during 2017.

We grew our new lending during 2017 by 12% to £4.5 billion, maintaining commercial and risk management discipline, while we improved our asset quality and have a fully loaded CET1 ratio of 14.7%. Our net interest margin remains strong at 2.02%, despite the backdrop of low interest rates and during 2017 we paid a further dividend to the Group of £160 million.

Our strategic partnerships

Our purpose is to be the leading partnership bank and to enable our partners, customers, colleagues and communities to thrive. Partnership remains a distinctive and important characteristic of our business strategy. We have grown and strengthened our relationships with our external partners, our internal partners, and customers. We work closely with all our partners in developing customer propositions, always seeking to secure improving benefits for all.

Our longstanding relationship with the Post Office remains a significant and important part of the Group's strategy with shared plans for a sustainable business that creates long term value. Through the Post Office Money brand, the Group provides easy access to a full range of retail financial products including savings, mortgages, loans, credit cards and ATM facilities for Post Office customers.

Our foreign exchange joint venture with the Post Office, First Rate Exchange Services Limited, is the largest provider of consumer foreign exchange in the UK. It has reported a further solid year of trading in an increasingly competitive market, which has been directly impacted by economic and geopolitical uncertainty. Through its digital applications First Rate Exchange Services Limited, provides ongoing innovation in the products and services supplied to our customers.

Our partnership with the AA in the UK has maintained its forward momentum. Both parties have worked together to successfully develop AA financial services propositions for AA members and the wider public through a new and enhanced range of retail banking products. After two years of trading the partnership has on-boarded over 150,000 new customer relationships and at year end had achieved a lending book of c.£350 million in assets, with strong and controlled growth in our personal loan offering.

Growing our mortgage business

The Group has a wide network of strategic distribution partnerships in the mortgage intermediary market, offering our products under both the Post Office and Bank of Ireland brands. Overall new mortgage origination across all channels increased c.15% to c.£3.2 billion, with a number of new and distinctive products launched during the year. As a business, we are focused on the needs of our customers and are maintaining our investments in innovative products, thereby addressing our customers ever changing needs and aspirations.

We have enhanced our operational capability through improvements in our processing technology and have introduced a new online mortgage service in November 2017 which allows mortgage offers to be available for brokers to view and download via the Group's award winning mortgage application system "Rome". For the second year running the Mortgage business was awarded five stars at the FT Advisor Online Innovation and Services awards.

Similar to many other players in the mortgage market, the Group found that managing redemptions during 2017 was challenging. The final redemption figure for the mortgage business was broadly in line with budget reflecting the Group's strategy and focus on retention and building mature customer relationships.

Building successful, sustainable businesses in Northern Ireland

Despite challenging market conditions with strong competition from established players and challenger banks, our Northern Ireland franchise increased its profit before tax by 6% to £53 million. This reflects strong margin performance, strict cost control and ongoing management of impairment charges on its commercial loan portfolio.

We closed six of our branches in 2017, reflecting the increasing move in customers' expectations for the delivery of financial services away from requiring branch premises and towards digital services, not just in banking but across all industries. This will contribute to ensuring the long term sustainability of this business, while ensuring we continue to meet our customer needs in a multi-channel and increasingly digital marketplace.

Northridge Finance & Marshall Leasing

Northridge Finance, our car and asset finance business, based in Northern Ireland but which delivers products and services to the whole of the UK market under the Northridge brand, had another excellent year. In what is a highly competitive sector, total business lending increased by 7% over 2016 levels to £1.5 billion. As part of the Group's growth strategy, in November 2017 Northridge Finance acquired a strategically important and complementary car and commercial vehicle leasing and fleet management company, Marshall Leasing Limited. I am delighted to welcome the Marshall team into the BOIUK family.

Great Britain Business Banking
The business banking operation in Great Britain, which is a historical business line and is being wound down, maintained its deleverage programme ahead of target with lending volumes now at £0.3 billion. The management of this business transferred in 2017 to our team in Northern Ireland.

Balance sheet and funding
During 2017 in line with its plans, the Group optimised its balance sheet position by growing its net lending by over £150 million and rebalanced its funding position accordingly. The Group is strongly capitalised, which will support its ambition for growth in the future.
The Group while still primarily retail deposit funded drew down from the Bank of England Term Funding Scheme and Indexed Long-Term Repo scheme during 2017.

Our partners, customers, colleagues and communities
The success of the Group would not be possible without our partners, the support of our customers and the commitment of our colleagues. Our purpose of being the leading UK partnership bank is centred on improving the behavioural values that we have prioritised including, do the right thing, strive for results, succeed together and relate to our customers.

I would like to thank our partners and our 2.9 million customers for their trust, loyalty and their business. They are the foundations of our success, and by continuing to support our customers and communities with easy, simple and accessible products we will endeavour to exceed their expectations and to deliver a brilliant experience to all.

During the year we sought and obtained feedback from our colleagues through an employee engagement survey to get insights on what matters to them. I would personally like to thank all my colleagues for this important feedback and also on their professionalism, determination, and commitment to the Group, its businesses and customers. During 2017 we have maintained our investment in, and support of our staff through skills training, supporting professional qualifications and career management. We are committed to a culture which respects and values diversity of qualities.

We continue to provide support for charitable organisations through "Give Together" and our other initiatives.

Board membership
There have been a number of changes in our Board membership over the last year and I would like to thank all my colleagues for their valued contributions during 2017.

The executive team was strengthened in the year with the appointment in March 2017 of Thomas McAreavey to the Board as Finance Director.

Amongst non-executive Directors, Peter Shaw, David Weymouth, Pat Butler and Lewis Love retired from the Board. I would like to thank Peter, David, Pat and Lewis for their diligence, support and counsel as Board members during the period. Furthermore in November 2017 we welcomed Mimi Kung to the Board and Risk Committee membership.

In October 2017, Ms Francesca McDonagh commenced her position as Bank of Ireland Group CEO, while Mr Richie Boucher stepped down. I would like to thank Richie for all his commitment to the Bank of Ireland Group and UK business and look forward to working closely with Francesca in the coming years in strengthening the UK business.

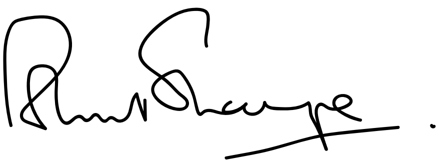
For my part, I have very much enjoyed working with the Board during my first full year. I look forward to another year of progress in 2018.

Outlook
In 2018 and beyond we are determined to build on the momentum made in recent years, making appropriate investments in our business and customer propositions while making further progress in embedding a strong risk management framework and improvements in our risk culture.

We will increase our focus on cost management, recognising the need for continual improvements in efficiencies in an increasingly competitive and dynamic market, where customer preferences and their interaction with us is changing.

We need to improve our agility to meet our customers changing needs and strive to maintain margins while offering value in customer products. All of this will enable us to continue to deliver sustainable returns to our shareholders.

Lastly, I would like to add my sincere thanks to the Executive team for their contribution, dedication and determination in delivering against the Group's objectives in 2017 and for the banks ongoing success. We are all committed to be the leading partnership bank which will enable our partners, customers, colleagues and communities to thrive.



Robert Sharpe
Chairman
6 March 2018

Strategic report

1.1 Purpose of the strategic report

The strategic report is a statutory requirement under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013, and is intended to be fair and balanced, and to provide information that enables the Directors to be satisfied that they have complied with Section 172 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 2017 and 31 December 2016.

1.2 Group key performance summary

	2017 £m	2016 £m
Operating profit before impairment charges on financial assets	143	181
Impairment charges on financial assets	(26)	(23)
Share of profit after tax of joint venture	34	35
Profit before taxation	**151**	**193**
Performance measures		
Net interest margin (%)	2.02%	2.07%
Average interest earning assets	23,386	24,053
Cost income ratio (%)	70%	63%
Segmental operating profit / (loss) before taxation[1]		
Great Britain Consumer Banking	134	165
Northern Ireland	53	50
Great Britain Business Banking	12	15
Group Centre	(48)	(37)
Profit before taxation	**151**	**193**
Impairment charges on loans and advances to customers		
Consumer	(15)	(4)
Residential mortgages	(2)	(2)
Non-property SME and corporate	(1)	-
Commercial property and construction	(8)	(17)
Total impairment charges on financial assets	**(26)**	**(23)**

Consolidated balance sheet and key metrics	**2017 £m**	2016 £m
Shareholders' equity	1,999	2,050
Total assets	26,235	25,960
Loans and advances to customers (after impairment provisions)	19,997	19,821
Customer accounts	18,961	19,475
Return on assets (%)	0.50%	0.63%

Definition of key performance measures

Net interest margin – is defined as net interest income for the year divided by average interest earning assets, net of specific provisions.

Average interest earning assets – is defined as the twelve month average of total loans and advances to customers, 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 expressed as a percentage of total operating income.

Return on assets – is calculated as profit after tax for the year divided by total assets, in line with the requirement in the European Union (Capital Requirements) Regulations (CRR) 2014.

[1] *Operating segments are defined on page 100.*

1.2 Group key performance summary (continued)

Capital	2017 %	2016 %
Common equity tier 1 capital ratio	14.7%	15.5%
Tier 1 capital ratio	17.7%	18.4%
Total capital ratio	20.5%	21.8%
Leverage ratio	6.6%	6.9%
Risk weighted assets (£m)	10,231	10,034

Liquidity	2017 %	2016 %
Liquidity coverage ratio[1]	127%	115%
Net stable funding ratio	130%	130%
Loan to deposit ratio	105%	102%

Capital ratios – capital ratios express the Group's capital as a percentage of its risk weighted assets and are calculated on a CRD IV fully loaded basis.

Leverage ratio – is calculated as the tier 1 capital divided by total balance sheet assets and off balance sheet exposures.

Risk weighted assets (RWAs) – on and off balance sheet assets are risk weighted based on the amount of capital required to support the assets. The Group adopts a standardised approach for calculating RWAs.

Liquidity coverage ratio (LCR)[1] – is calculated as the high quality liquid assets, divided by net cash outflows over the next 30 days, expressed as a percentage.

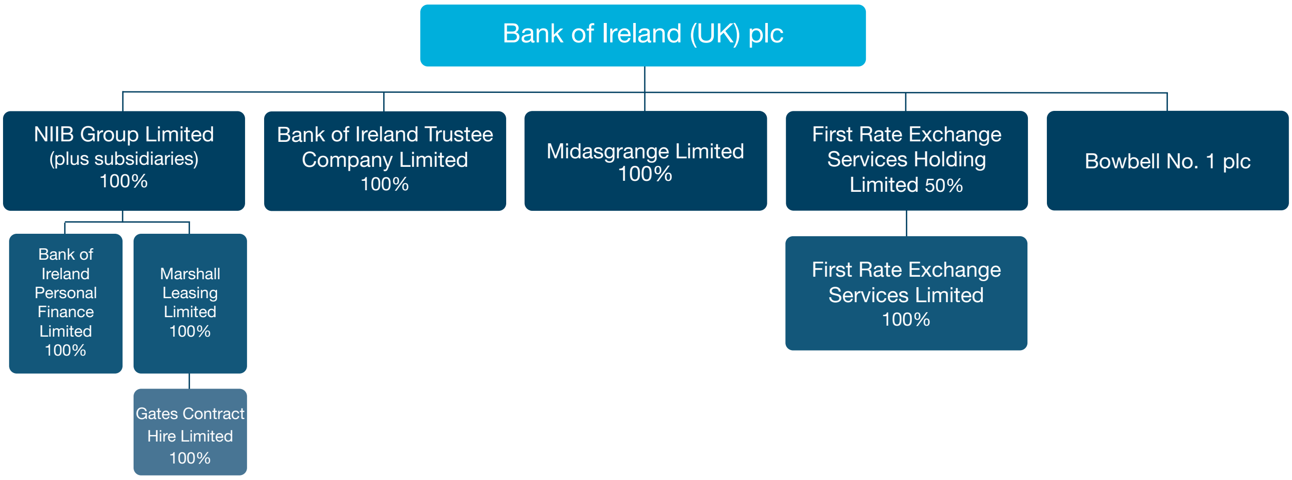
Net stable funding ratio (NSFR) – is defined as the total amount of available stable funding divided by the total amount of required stable funding, expressed as a percentage.

Loan to deposit ratio – is defined as loans and advances to customers expressed as a percentage of customer deposits.

In addition to the key performance measures set out in this section, other key performance measures are discussed in section 1.7.

[1] *The Group's Liquidity coverage ratio is calculated based on the Commission Delegated Regulation (EU) 2015/61 which came into force on 1 October 2015.*

1.3 Group structure



At 31 December 2017, the Group consisted of Bank of Ireland (UK) plc (the 'Bank') and its share in the entities as shown above. A summary of each shareholding is as follows:

- 100% of NIIB Group Limited (NIIB) – an asset finance and consumer lending group trading as Northridge Finance.
- On 24 November 2017, NIIB Group Limited acquired 100% of the ordinary share capital of Marshall Leasing Limited (MLL) from the entity's parent company, Marshall Motor Holdings plc (Refer to note 20). MLL is a car and commercial vehicle leasing and fleet management company based in Cambridge in the United Kingdom. MLL owns 100% of the ordinary share capital of Gates Contract Hire Limited which is a dormant company.
- On 15 September 2017, Northridge Finance Limited, a dormant subsidiary of NIIB entered member's voluntary liquidation.
- 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 the Post Office.
- 100% of Bank of Ireland Trustee Company Limited – this company ceased trading in February 2014.
- 100% of Midasgrange Limited – this company traded as Post Office Financial Services until 3 September 2012 when the trade, assets and liabilities transferred to the Bank.
- Bowbell No. 1 plc (Bowbell) - an 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 IFRS 10 (Refer to note 38).

The Bank is a public limited company incorporated in England and Wales and domiciled in the UK.

The Group is regulated by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).

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

1.4 UK economic and market environment

UK economic and market environment
The performance of the UK economy in 2017 was broadly in line with market expectations with GDP growth estimated to be c.1.8%, a slightly more subdued outcome compared to recent years in what is now a mature recovery. Political developments again cast a shadow following the outcome of a snap general election, the beginning of EU withdrawal negotiations and heightened uncertainties over the likely shape of the post-Brexit UK economic landscape.

Despite these developments, the labour market continued to demonstrate resilience with unemployment falling to a 42 year low of 4.3% and the employment rate rising to a new recorded peak above the 75% level during the year. Wage growth however remained relatively muted at around 2% on average, as the general recovery in productivity performance across the economy continued to disappoint.

A key development during 2017 was the revival in retail inflation with the target CPI measure reaching a six year high of 3.1% in November, largely reflecting rising costs from the impact of the significant depreciation in the sterling exchange rate after the 2016 EU referendum.

2017 also saw the first increase in the Bank rate in a decade, with the Monetary Policy Committee effectively reversing the 25bps cut that was judged appropriate in the aftermath of the EU referendum in 2016. However, the immediate impact on the market was limited reflecting the changing pattern of borrowing and stronger preference for fixed rate products in recent years.

Growth in our key markets
Housing market developments continued to mirror those of the wider UK economy in 2017, slightly subdued and with some parts doing better than others. Overall, average house prices ended the year just over 2.5% higher on some indices[1], representing a modest deceleration in the pace of growth compared to recent years. Total residential transactions were estimated at c. 1.2 million, slightly below 2016 levels with arrears and possessions

[1] *Nationwide, Halifax House Price Indices (January 2018)*

1.4 UK economic and market environment (continued)

across the market remaining low but marginally up on the previous year. Gross mortgage lending was estimated by UK Finance to have reached £248 billion, the highest since 2008.

Price competition remained intense in the mortgage market, supporting a shift in the mix of borrowers towards both first-time buyers and, as the year progressed, stronger refinancing activity. Government schemes such as the Help to Buy equity loan helped boost the numbers of those seeking a foot on the ladder while record low interest rates and the prospects of policy change encouraged a rise in the number of loans for remortgage. The home-mover segment continued to be less vibrant, limiting the supply of properties coming on the market. Regional variations in performance were again evident with the London and South-East market experiencing a more muted performance relative to other parts of the UK where affordability seemed less stretched.

Regulatory and fiscal changes, including the first stage of a four year transition on tax relief and the change in stamp duty for additional homes continued to reduce confidence and dampen activity in the buy-to-let market, continuing a trend that commenced in 2016. The significance to the market of the change to stamp duty for first time buyers announced in the November budget remains to be seen.

Consumer credit growth continued to significantly outpace the wider economy during 2017 although there was some evidence that the strength of demand may have eased slightly in the second half of the year, consistent with more cautious trends in household spending and as the market responded to pronouncements on risk from the Regulator. The growth in personal deposits also slowed to c. 2% year on year, with some signals that consumers were partly sustaining spending by utilising savings.

After a five year period of consistently strong year on year growth, a combination of cyclical and structural factors impacted demand for new cars in 2017, resulting in the weakest year for new registrations since 2011. By December 2017, Society of Motor Manufacturers and Traders (SMMT) reported new registrations were down 5.7% year on year. In contrast, the market for used cars and associated demand for finance proved more resilient with a broadly steady performance reported in 2017.

Despite a political impasse, the absence of devolved government and particular Brexit-related uncertainties, the regional economy in Northern Ireland had a steady year with growth rates slightly below with the UK overall. While rising inflation presented a more difficult climate for households, SME activity levels remained positive with the lower exchange rate boosting cross-border retail flows, strong tourism numbers and manufacturing exports. The region continued to attract Foreign Direct Investment (FDI) while both residential and commercial property sectors enjoyed a steady year, helping sustain demand for both mortgage and business finance.

Outlook for 2018

2017 ended on a positive note with the EU agreement that “sufficient progress” had been made to allow negotiations to move on to a possible transition agreement and longer-term trade deal. This would appear to have reduced the risks of a disorderly exit from the EU although significant uncertainty remains and in doing so may underpin economic confidence in the year ahead. While the possible long-term impacts on the UK economy remain difficult to predict, as a primarily retail funded and UK domestic focussed bank, the Group will continue to evaluate and respond to the emerging risks and opportunities from a changing external environment.

While all forecasts carry even more uncertainty than usual in the current environment, the consensus expectation is that UK GDP growth will continue in a lower gear in 2018, unemployment will remain low but will rise modestly and consumer inflation pressures will ease gently back towards the 2.0% target. While there are some tentative signs of upward pressure on wages, overall the squeeze on real earnings is expected to continue for much of the year representing a continued headwind to growth in household discretionary spending.

Levels of business investment are likely to remain sensitive to fluctuating Brexit-related sentiment but the prospects for manufacturing exports seem brighter, aided by a more optimistic outlook for growth in key global markets and the competitive exchange rate.

Residential and Commercial property prices and activity levels are expected to be broadly stable in the year ahead although with significant regional variations. The affordability stretch and supply constraints are more prominent in some areas than others. The market waits to see what impact, if any, the reform to stamp duty and measures to boost supply (as announced in the November Budget) will have on the market. First Time Buyers are again likely to outnumber home-movers while buy-to-let activity may remain subdued in the near term. The Group will continue to support these customers who want to own their own home and is continually innovating to develop products to meet customers needs.

Another modest tightening of monetary policy is expected during 2018 with the Monetary Policy Committee seeking to bring inflation back towards the 2% target. The magnitude and timing of any interest rate increases are likely to be influenced by the pace of wage growth.

If the economy evolves in line with the consensus view, the Group would expect growth across our markets to be broadly stable in aggregate although the pace of growth in consumer credit may continue to decelerate from the double-digit percentage rates of recent years. This is a segment of market where the Regulator has highlighted “pockets of risk”.

As reflected in the latest Office for Budget Responsibility outlook which accompanied the Budget, the medium term prospects for the UK economy, fiscal targets and average living standards are likely to remain quite challenging in the absence of a more vigorous recovery in productivity.

In uncertain times the Group will continue to monitor the resilience of the economy and changing behaviours but the priority remains to provide high quality products and services to our customers through our respective partnerships and franchise business in Northern Ireland.

1.5 Our business strategy and goals

- The Group's vision is to be the leading partnership bank providing simple, flexible, accessible financial services and products to UK customers, both directly and through partnerships with trusted, respected UK brands and intermediaries, thereby providing attractive, sustainable returns to our shareholder.
- The Group is organised into operating business units to service its customers brilliantly: Great Britain Consumer Banking, Northern Ireland, Great Britain Business Banking and Group Centre.
- The Group's central functions establish and oversee policies and processes, while the Group also leverages the overall scale and capability of its Parent in support of its strategies. Certain functions including but not restricted to product manufacture, customer service and IT are provided by the Parent under a Master Services Agreement.

Whilst the Group's strategy remains unchanged, it is acknowledged that an increasingly competitive, fast moving and uncertain environment will necessitate flexibility to achieve planned financial outcomes. In conjunction with its Parent, the Group has an extensive IT plan and a multi-year investment programme which will support IT and payment application upgrades.

The Bank of Ireland Group is focused on delivering three key strategic priorities:
- **transforming** the Group's culture systems and business model;
- **serving customers brilliantly**; and
- **growing sustainable profits** and returns for shareholders.

These priorities are incorporated within the strategic vision of the Group as set out below.

Strategic vision	Strategic priorities delivered through	Key performance measures	Addressing principal risks[1]
Growth in Great Britain Consumer Banking through partnerships with Post Office and AA	Building a sustainable consumer banking franchise by further growing the complementary Post Office and AA financial services relationships and other strategic partnerships. Optimisation of the Group's consumer lending strategy.	Income, net interest margin and profit before taxation (including segmental performance) - applies to all aspects of the Group's strategic plan with actual performance compared against plans and prior periods.	• Credit risk • Liquidity & funding risk • Market risk • Regulatory risk • Operational risk (including legal risk and outsourcing) • Business / Strategic risk • Reputation risk • Capital adequacy risk • Conduct risk
Growth in Northern Ireland and sustained profitability	Improving the operating profitability and new business levels of the business, by supporting our customers and the Northern Ireland economy.	Effective management of funding requirements through a mix of customer deposits and wholesale funding to support the growth in lending volumes, with continued discipline on pricing.	
Product & Service Development: serving customers brilliantly	Transforming the customer journey and experience through technical innovation, digitisation and product development; ensuring that we are fair, compliant and accessible, as set out in the Group's Customer Charter.	Conduct Compliance Key Risk Indicators.	• Credit risk • Regulatory risk • Operational risk (including legal risk and outsourcing) • Business / Strategic risk • Reputation risk • Conduct risk
Sustainable Returns within Risk Appetite	Generating sustainable returns from existing and new business, that are aligned with the Group's risk appetite and that achieve the required return on capital for the shareholder, with increased focus on cost efficiency.	• Profitability, capital, liquidity and funding ratios • Cost income ratio • Conduct Compliance Key Risk Indictors	• Capital adequacy risk • Credit risk • Liquidity & funding risk • Market risk • Regulatory risk • Business / Strategic risk • Conduct risk

Working in partnership with our customers and stakeholders is core to all that we do.

The Group's core values form part of our culture and include:
- **Doing the right thing** - strive to do what is best in the long term for each other, our partners, customers and communities;
- **Relating to our customers** - by transforming the customer journey and experience through creativity, innovation and putting customers at the heart of our decision-making;
- **Succeeding together** - by actively sharing and collaborating internally and with our stakeholders to achieve our mutual objectives; and
- **Striving for results** - being committed, focused and empowered to deliver quality, sustainable results for ourselves and our stakeholders.

We deliver simple, flexible and accessible financial services products through partnerships with some of the most respected and trusted brands in the UK and directly through our full service banking operation in Northern Ireland. Our car and asset finance business,

[1] *Principal risks and uncertainties are detailed further in section 1.8.*

1.5 Our business strategy and goals (continued)

Northridge Finance, has also developed strong partnerships with market leading dealers and franchises and has enhanced its product offerings this year with the acquisition of MLL. The mortgage business offers a wide product range via an extensive number of strategic mortgage intermediary partnerships.

Great Britain Consumer Banking
Great Britain Consumer Banking offers deposits, mortgages, credit cards, loans (including car and asset finance) and personal current accounts under Bank of Ireland UK, the Northridge and Marshall (MLL) brands and through partnerships with the Post Office, AA and intermediaries.

The strategic priorities for Great Britain Consumer Banking are:

- to put the customer at the centre of everything we do;
- to build a strong consumer banking franchise through strategic partnerships and distribution channels;
- to establish a profitable back book through retention of mortgages and deposits; and
- to develop enhanced IT capability and customer value propositions across the business, growing income returns.

Post Office partnership
The Group has an exclusive financial services partnership with the Post Office under a contract that currently covers the period until 2023. The Group partners with the Post Office to offer products online and through a distribution network of over c.11,500 Post Office branches in the UK serving c.2.4 million customers, offering a range of products including mortgages, savings, credit cards, personal loans and current accounts.

The Post Office is primarily responsible for sales performance and marketing, while the Group is responsible for product development, pricing and service delivery.

Post Office personal loans had a successful year, welcoming over 10,000 new customers, equating to over £100 million in written lending at the end of 2017. As part of the Group's goal to serve customers brilliantly, investments in the personal loan propositions during 2017 delivered many improvements for our customers, including faster funds issuance and easier and improved interaction.

Through the Post Office network there are c.2,400 free to use ATMs which completed c.230 million transactions and dispensed c.£10 billion of cash during 2017. This network represents c.3.5% of Link ATMs and covers c.6% of all transactions in the UK Link network.

FRESH, the Group's foreign exchange joint venture with the Post Office has, through its wholly owned subsidiary FRES, maintained its position as the number one provider of retail travel money in the UK providing retail and wholesale foreign exchange services, with c.24% UK market share and over one million travel money prepaid cards sold and 500,000 mobile apps downloaded, where customers can upload funds and check balances via their mobile devices.

The Post Office launched the 'new' Travel Money Card on 7 March 2017. This card is contactless, has the ability to load 13 different currencies and it can also be linked to the current mobile app. This product gives the Post Office a market leading prepaid Travel Card.

The same day Click and Collect currency service which was launched in 2015 has continued to be successful as an easy and convenient way to purchase travel money. It has now been extended to 3,700 Post Office branches.

During 2017, various Post Office products continued to win awards for their motivation, simplicity and competitive position.

This included the award for "Best Overall Personal Finance Provider" at the prestigious Personal Finance awards, and recognition as the "Best Foreign Exchange Provider" at the British Travel Awards, building on the silver award in the previous year.

AA partnership
In July 2015 the Group announced its partnership with the AA for a minimum period of ten years. The AA is regarded as one of the best known and trusted brands in the UK and the largest provider of roadside assistance services, representing 40% of the UK breakdown market with over three million members. This partnership aims to provide an enhanced range of products to AA members and the wider public, combining the Group's proven product development capabilities with the strength of the AA brand and broader business assets.

Under the AA brand, credit cards, savings, personal loans and mortgage products are offered to customers.

After two years of trading the AA partnership has on-boarded over 150,000 customers and has achieved a lending asset book of c.£350 million at December 2017 which is primarily funded by AA originated customer deposits.

In September 2017, a "Which?" survey recommended AA in joint second place for Best Financial Services Brand based on highly competitive deals in multiple categories and a customer score of 70% in relation to customer service, transparency and dealing with complaints.

Mortgages
The Group offers residential and buy to let mortgages directly through the Post Office, the Bank of Ireland NI branch network, and also through partnerships with numerous leading mortgage intermediaries under both Post Office, the AA, and Bank of Ireland UK brands.

The Group has an established history in the UK mortgage industry and since 2014 has successfully secured strategic partnerships with a number of leading mortgage intermediaries as it looks to provide more choice and expertise to customers.

Over recent years substantial investment has been made in developing technology and recruiting new teams with significant intermediary mortgage experience as the Group strives to continually improve the customer experience. In 2017 various new mortgage propositions were developed and launched. Mortgage redemptions were actively managed and in line with plan, with low levels of loan losses recorded.

New product propositions included a 95% loan to value mortgage range (with the aim of providing support to those who can no longer benefit from the Government's Help to Buy scheme), and other propositions for first time buyers. The Group also provides competitively priced fixed rate products across a range of loan to value bands.

In November 2017, to enhance customer functionality a new online service was launched which allows mortgage offers to

1.5 Our business strategy and goals (continued)

be available for brokers to view and download via the Group's multi award winning mortgage application system ("Rome").

For the second year running the UK Mortgage business was also awarded five stars at the FT Advisor Online Innovation and Services awards. Other awards for mortgages in 2017 included the "Best Fixed Rate Mortgage Lender" at the What Mortgages Awards as well as being shortlisted for the following MoneyAge awards:

- Innovation in Consumer Finance Award;
- Mortgage Provider of the year; and
- Bank / Building Society of the year.

In addition to the Post Office Mortgage business rolling out its new model for selling mortgages through 120 Post Office branches in 2016, earlier in 2017, the Bank joined the Personal Touch Mortgage (PTM) panel. PTM is a highly respected network of intermediaries which now has more than 300 members and 580 advisers across the UK. The full range of the Group's mortgage products will be available via this network, backed by "Rome".

Northridge Finance

The Group, through its Northridge Finance brand provides personal and commercial finance serving the Motor, Agricultural and Insurance Premium Finance markets with total lending at December 2017 of £1.5 billion.

Northridge Finance is one of the UK's most dynamic and partner driven finance houses offering a comprehensive range of lending products and services for the dealer and intermediary market which can be used to best meet individual customer requirements. The Group's strategy is to grow its market share within the motor dealer and asset finance intermediary markets and in the direct business to business market, while maintaining excellent asset quality.

As part of the Group's growth strategy, on 24th November 2017, NIIB Group Limited acquired 100% of the ordinary share capital of Marshall Leasing Limited (MLL) from the entity's parent company, Marshall Motor Holdings Plc. MLL is a car and commercial vehicle leasing and fleet management company.

MLL's business model involves the outright purchase of vehicles which are subsequently rented out on a contract hire arrangement, currently to SME customers.

The purchase of MLL opens up a strategic opportunity to leverage the systems and experience within MLL to deliver personal contract hire to customers through the Group's Partnership Bank distribution channels.

Northridge Finance has won three prestigious industry awards over the past three years, most recently being voted the "Best Independent Bank Owned Lender" at the Car Finance Awards in June 2017. MLL won the "Leasing Company of the Year" at the Association of Car fleet Operators annual awards in November 2017.

Northern Ireland

The strategic priorities for the Northern Ireland business are:

- to become the leading bank in Northern Ireland for customer service;
- to deliver sustainable growth through the Northern Ireland Branch and Business Centre Network; and
- to increase market share of Northern Ireland business lending.

The Northern Ireland business offers a comprehensive range of banking products for retail and SME businesses serving nearly half a million customers, through a distribution network of 28 branches (including six business centres), central support teams, ATMs and direct channels (telephone, mobile and on-line). The Bank is also one of four banks authorised to issue bank notes in Northern Ireland.

2017 saw the further implementation of the Northern Ireland strategic review with the closure of six branches. The strategic imperative is to continue to invest in digital infrastructure to allow the development of competitive digital propositions and integrating all distribution channels is seen as key to future growth.

The Northern Ireland business core capability and strength lies in the quality of its people and their customer relationship management capability.

The Northern Ireland business continues to be profitable and this primarily reflects improved funding costs, efficient cost control and ongoing management of impairment charges on its commercial loan portfolio. Investments have also been made to upgrade and modernise the branch network, including self-service propositions.

The Group continued its highly successful Enterprise Programme, which is now in its sixth year, to help support SMEs in their own communities, including the Enterprise Weeks held in May and November 2017.

In October 2017 the Group launched the Innovation Matters programme aimed at supporting communities through a focus on teachers and students to enchance skills needed for technological revolution. The programme includes giving schools free access to the MakeMatic bite sized professional learning videos, the BoI Junk Kouture Fashion and Arts competition, the Young Enterprise Tech programme, where students have the chance to set up and run their own tech company and Generation Innovation which increases young people's awareness of future careers as innovators.

The Bank was awarded 5 star ratings for three business current accounts in Northern Ireland by Moneyfacts a provider of personal financial information.

Great Britain Business Banking

Under the amended EU Restructuring Plan announced on 9 July 2013, the Parent committed to exit its Great Britain Business Banking and corporate banking businesses. In 2017, the management of all remaining Great Britain Business Banking lending was centralised in Northern Ireland, with the mandate to continue to manage these reducing portfolios over the coming years.

This strategy for Great Britain Business Banking does not impact on the Group's Consumer Banking businesses including its partnerships with the Post Office and the AA, nor its activities in Northern Ireland.

The reduction of the Great Britain business banking business continues to release capital and funding, which will be used to fund growth primarily in the consumer business.

Capital

The Group's strategy is to optimise its capital position and capital returns and seek new lending and other business opportunities, in both commercial and consumer business, which are aligned with its risk appetite.

During 2016, the first equity dividend of

1.5 Our business strategy and goals (continued)

£220 million was paid to the Parent. In 2017 a further dividend of £160 million was paid.

On 19 December 2017 a capital restructure took place to repurchase £135 million of Tier 2 subordinated debt, financed by the Group's Own Funds. Subsequently, £90 million of new subordinated Tier 2 debt was issued. After the transaction the capital ratios of the Group exceeded the minimum capital requirements outlined in the CRD IV/ CRR.

Liquidity
The Group is authorised by the PRA and is subject to the regulatory liquidity regime of the PRA.
At 31 December 2017 the Group continues to maintain a sufficient liquidity and funding position and is fully compliant with all liquidity and funding obligations with an efficient funding profile maintained during the year. At 31 December 2017 the Group has a loan to deposit ratio of 105% and an LCR of 127%.

CRD IV rules in relation to other regulatory liquidity requirements including NSFR and Additional Monetary Metrics are yet to be finalised by the regulator. Preparations are underway to ensure the Group is in a position to meet the finalised requirements.

The Group actively monitors its liquidity position using various measures including LCR and NSFR and takes these into account in the creation, execution and review of its funding plans.
In August 2016 the Bank of England launched the Term Funding Scheme (TFS) as part of a UK monetary stimulus programme in the wake of the result of the UK referendum on membership of the EU. TFS provides banks with a cost effective source of funding in the form of central bank reserves to support additional lending to the real economy, in exchange for eligible collateral.

The Group has availed of this funding as part of its effective balance sheet management and to improve the overall funding mix. As at 31 December 2017 the Group had drawn £1.2 billion from TFS, which will be repaid by 2021.

1.6 Corporate social responsibility - customers, colleagues and communites

Aligned to our Parent's core purpose, the Group's corporate social responsibility activities are evidenced through ongoing developments which enable our **1. Customers**, **2. Colleagues** and **3. Communities** to thrive. Specific initiatives under these three headings are described below. Our Parent's annual Responsible Business Report can be viewed at www.bankofireland.com.

1. **Customers**
   Within the Partnership strategy, a core value for the Group is 'Relate to Customers'. This helps colleagues to put the customer first, aim to get things right for the customer first time, focus on customer relationships, make the best customer decisions, understand what our customers need and continuously seek to improve the overall customer experience.

   The Group has responded 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, and particularly in the following two areas:

   - ***Vulnerability***
     Vulnerability is about making reasonable adjustments and appropriate provisions for customers or their representatives with particular needs. The Group continues to run a dedicated Consumer Vulnerability Programme, and has delivered a number of initiatives, including the appointment of Vulnerable Customer Champions from across the Group, specialist training for Champions and key customer-facing staff, the introduction of a mandatory online training programme, the development of new identifying and signposting guidance for external support providers, and the launch of a suite of new online customer assistance tools across the Group and its partners' websites.

   - ***Customer Understanding***
     The Parliamentary Commission on Banking Standards Changing Banking for Good Report has highlighted and placed the need for more emphasis on the treatment of customers, in particular, how banks assess that customers fully understand that they have bought the right products.

     The Group has responded by commencing periodic research to test customers' overall understanding to ensure they have taken out the right product for their needs.

     This approach is also underpinned by the Group's Customer Charter which covers key commitments and promises to our customers and partners.

     The objectives of the Customer Charter are:

     - To identify customers' needs and provide clear and affordable value for money products to meet customer expectations;
     - To provide friendly, efficient and relevant services;
     - To be committed to establishing and maintaining long term customer relationships; and
     - To provide quality of service with clear and consistent communication to customers.

   In accordance with relevant UK legislation, the Group has published its statement on Modern Slavery and Human Trafficking for 2017. The Statement sets out the steps and measures the Group has taken to seek to ensure that modern slavery and human trafficking does not occur within its supply chain or in its business operations. A copy of the statement is published on the Parent website and can be viewed or downloaded at www.bankofireland.com.

   In 2017 the Group has continued to see a low level of referrals to the ombudsman by customers dissatisfied with the outcome of any complaint. The Group is building on this position to ensure that when issues arise they are dealt with quickly and effectively to ensure a positive and fair outcome for customers at all times. We have also sought the opinion of customers via surveys, taking output and learnings to make continuous improvements across our business.

1.6 Corporate social responsibility (continued)

2. Colleagues

The current and future success of the Group in achieving its strategic priorities depends on having a continuous focus on:

- talent and capability development;
- engaging our workforce;
- managing business change;
- supporting the regulatory agenda; and
- articulating our culture

This will enable the Group to succeed together as the Partnership Bank. The Group is committed to investing in its people to ensure they can effectively support customers, deliver the Group's strategic priorities and develop their individual careers. In 2017, over 25,977 training hours were completed by UK employees.

Be At Your Best, the Group's personal development and wellbeing programme, which focuses on career, mind and body, saw over 2,000 employees participate in a range of initiatives, including HeadShed, Couch to 5k and Career Fairs.

The Group has continued to bring its unique Partnership Bank Strategy and Values to life for colleagues who work in and support the business. Following a series of events held at the end of 2016 and early 2017, when more than 2,000 colleagues attended one of 14 'Partnership Bank Live' events held in five different UK locations and in Dublin, the Group has continued to engage and embed its strategy, purpose and values via its employee brand, Living Partnership. This has been achieved through a range of activities including employee events, employee recognition awards, workshops, focus groups and surveys, and ongoing engagement with more than 300 'Shapers', colleagues who are actively supporting our partnership journey. The Group's office environments in London, Bristol and Belfast have been updated to reflect and advocate the partnership ethos and encourage creativity and engagement.

The Group seeks to operate at the highest ethical standards by encouraging an environment where doing the right thing is embedded in the core of the organisation. The Group has clear expectations for behaviour and conduct with an annual mandatory training programme for all employees.

The Group Code of Conduct sets the standards of ethical behaviour to create the right culture and the following standards and behaviours are expected from all employees:

- to act with integrity and honesty;
- to report wrongdoing;
- to avoid disclosing confidential information;
- to avoid conflicts of interest; and
- to comply with legislation and regulations.

The Group believes that by applying these standards, all colleagues can make sound decisions and, when faced with complex dilemmas achieve good outcomes for all our stakeholders.

To help ensure that the Code of Conduct is embedded in every aspect of the business, the Group encourages and supports employees to speak out if they witness wrong doing, such as a breach, or suspected breach, of the Code of Conduct standards, or any concern they might have in respect of potential improprieties.

Employees not only need to perform their duties with honesty and integrity, they also have to be seen to do so. To help them avoid compromising their ability to perform their everyday duties with honesty and integrity, the Group has developed arrangements to help manage potential or actual conflicts of interest.

The Group has defined and implemented policies, standards, and procedures to ensure that it operates to the highest of standards, both from the perspective of the Group's legal, regulatory and compliance requirements, and also in an ethical, fair and consistent manner. The Group's policies and standards set out clearly the Group's objectives and provide direction to its staff, management, and Board in carrying out their various day-to-day activities.

As well as supporting customers to avoid attempts by fraudsters to steal their account details, the Group is also aware of the importance of keeping the customer information we hold as safe and secure as possible, while complying with relevant data protection legislation. Employees, across all jurisdictions, are required to complete training on information security each year to ensure that they are aware of how to keep customer information private and secure and to avoid breaches of data protection.

3. Communities

The Group strives to make a positive contribution in the communities where it operates. Employees are actively involved in fundraising and volunteering in charitable events across the UK. In 2017, the Group, with employee endorsement, chose Alzheimer's Society UK as its flagship charity for 2017-18. During 2017 the Group raised £146,000 for the Alzheimer's Society's Side by Side programme, which offers free, one-to-one support for people with dementia, helping them to continue to do the things they love.

In addition, colleagues have continued to raise funds for charities close to their heart through our Give Together programme. Give Together is the Group's charity and community initiative, through which staff lend their support to their nominated charities by fundraising, volunteering and making donations. The initiative provides paid leave for volunteering and matches fundraising awards.

The Group is proud to support a wide range of Northern Ireland based community, business and sporting activities through sponsorship each year. Open Farm Weekend is one such event which the Group has sponsored since 2012. The annual event aims to raise awareness of food production and the local supply chain in Northern Ireland.

The Group has also launched Innovation Matters, a new programme that will provide a wide range of free initiatives and resources to schools across Northern Ireland to help prepare students for life in a technology transformed world.

Our Parent continues to provide the Group with products and services to ensure the environment across the business is managed responsibly. Environmental initiatives which have been delivered this year include certification to ISO50001 energy management standards, the installation of smart meters and compliance with energy regulations.

1.7 Financial review

1.7.1 Summary Group consolidated income statement

	2017 £m	2016 £m
Net interest income	471	497
Net other income	-	(3)
Total operating income	**471**	**494**
Operating expenses	(328)	(313)
Operating profit before impairment charges on financial assets	**143**	**181**
Impairment charges on financial assets	(26)	(23)
Share of profit after tax of joint venture	34	35
Profit before taxation	**151**	**193**
Taxation charge	(21)	(29)
Profit for the year	**130**	**164**

1.7.2 Net interest income

Net interest income / Net interest margin	2017 £m	2016 £m
Net interest income	471	497
Average interest earning assets	23,386	24,053
Net interest margin (%)	2.02%	2.07%

Net interest income for the year ended 31 December 2017 was £471 million compared to £497 million for the year ended 31 December 2016.

The reduction in net interest income of £26 million was impacted by:

- changes in fair value unwind assumptions on the acquired mortgage portfolio, which have resulted in a £17 million reduction in income year on year; and

- a £12 million effective interest rate adjustment on the core mortgage portfolio, where the estimated standard variable rate reversionary period reduced by two months.

Gross interest income was £651 million (2016: £762 million) and consisted principally of interest earned on customer lending and on amounts placed with the Parent.

Gross interest expense was £180 million (2016: £265 million) and primarily represented interest paid or payable on customer deposits and on amounts borrowed from the Parent.

The Group's net interest margin has remained consistently above 2% despite challenging market conditions and the low interest rate environment.

The net interest margin in 2017 reduced by 5 basis points to 2.02% mainly due to:
- reduced income on the acquired mortgage portfolio. This reduction was due to the average life of certain loans being longer than initially anticipated which impacts on the timing of interest income recognised over the life of that loan (Refer to critical accounting estimates and judgements on page 98);
- changes in effective interest rate (EIR) assumptions on the mortgage and credit cards portfolios;
- ongoing repayments on higher margin variable mortgages;
- the continued proactive deleverage of the GB commercial book;
- offset somewhat by reduced Post Office deposit and other funding costs;
- the growth in income from the personal lending portfolio; and
- increased income from Northern Ireland products.

1.7.3 Operating expenses

Operating expenses	2017 £m	2016 £m
Staff costs	54	39
Other costs	274	274
Operating expenses	**328**	**313**

The majority of the Group's cost base relates to outsourced services, being the costs of distribution, product manufacture and support provided by the Parent under various contractual arrangements. The year on year increase in staff costs of £15 million reflects the reallocation of mortgage business staff costs under outsourcing arrangements to the Parent and which were previously disclosed under other costs.

Overall operating expenses increased by £15 million in 2017, largely reflecting increased new business volumes in personal loans and mortgages while the Group also continues its commitment to invest in its people, technology, regulatory compliance and business growth. The increase in expenditure was somewhat offset by cost efficiencies across the business.

The aforementioned investments enabled enhanced product offerings for partners and customers during 2017 and the Group expects to leverage this investment during 2018 with futher product launches and volume growth.

1.7.4 Impairment charges on loans and advances to customers

Impairment charges on loans and advances to customers	2017 £m	2016 £m
Consumer	15	4
Residential mortgages	2	2
Commercial property and construction	8	17
Non-property SME and corporate	1	-
Total impairment charges on loans and advances to customers	**26**	**23**

The impairment charge for the year ended 31 December 2017 on loans and advances to customers was £26 million, compared to £23 million for the year ended 31 December 2016.

Year on year movements by lending portfolio are detailed below:

- The £11 million increase in impairment charges on the consumer portfolio largely reflects the planned growth and maturity profile in personal loans which were relaunched in Post Office and AA during 2016.
- Impairment charges on the residential mortgage portfolio remain flat year on year.
- Commercial property and construction impairment charges reduced by £9 million as a result of continued improvement in the commercial and residential property sectors and successful recovery activities and the benefit of an Incurred But Not Reported (IBNR) provision release.
- Non-property SME and corporate impairment charges increased by £1 million year on year.

All loan portfolios remain sensitive to economic changes and the uncertainty as the UK plans to leave the EU. However, the low interest rate environment has somewhat increased customer confidence.

Refer to sections 2.1.6 and 2.1.7 of the Risk Management report for further credit risk details in relation to loans and advances to customers.

The estimated quantitative impact on initial adoption of IFRS 9 is a reduction in shareholders' equity of c.£40 million after tax, substantially all of which relates to an increase in impairment loss allowance on loans and advances to our customers.

Further information on IFRS 9 implementation is included in the Risk Management section on pages 53 to 55.

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1.7.5 Taxation charge

The taxation charge for the Group was £21 million for the year ended 31 December 2017 compared to a taxation charge of £29 million for the year ended 31 December 2016.

Excluding the £34 million (year ended 31 December 2016: £35 million) income from the Group's joint venture, FRES, the effective tax rate for the year ended 31 December 2017 was 18% (year ended 31 December 2016: 18%).
The effective tax rate is influenced by a number of factors, including:

- the fair value unwind on acquired mortgages, as discussed in the Group Accounting Policies on page 98, which is non-taxable in the Group; and
- the 8% corporation tax surcharge for banks which came into effect from 1 January 2016.

Refer to note 11 and note 23 respectively for further information on the taxation charge and deferred tax asset at 31 December 2017.

The Group has disclosed its UK tax policy in line with Schedule 19 of the UK Finance Act 2016, on its website www.bankofirelanduk.com.

1.7.6 Summary consolidated balance sheet

	2017 £m	2016 £m
Cash and balances with central banks	1,836	1,172
Loans and advances to banks[1]	2,764	3,369
Loans and advances to customers	19,997	19,821
Available for sale financial assets	1,008	1,140
Total other assets	630	458
Total assets	**26,235**	**25,960**
Deposits from banks[2]	3,561	2,691
Customer accounts	18,961	19,475
Subordinated liabilities	290	335
Total other liabilities	1,424	1,409
Total liabilities	**24,236**	**23,910**
Total equity	1,999	2,050
Total equity and liabilities	**26,235**	**25,960**
Loan to deposit ratio	**105%**	**102%**

1.7.7 Loans and advances to banks and deposits from banks

Since 2013 the Group has adopted a derivative hedging approach to manage interest rate risk with c.£1.3 billion (2016 : £2.0 billion) of legacy gross flow cash hedges (originated prior to 2013) remaining on the balance sheet at December 2017 and included under loans and advances to banks and deposits from banks.

Over time, the remaining gross flow cash hedging deals with the Parent will continue to be replaced by derivative contracts with the Parent.

Deposit from banks increased in the year, primarily reflecting the net impact of increased drawings from TFS / ILTR offset by the aforementioned reduction in legacy gross flow cash hedging deals of £0.7 billion.

1 Included in loans and advances to banks is a balance due from the Parent of £1.4 billion (31 December 2016: £2.0 billion) and £1.4 billion (31 December 2016: £1.3 billion) due from external bank counterparties. Refer to note 14.

2 Included in deposits from banks is a balance due to the Parent of £2.0 billion (31 December 2016: £1.9 billion) and £1.6 billion (31 December 2016: £0.8 billion) due to external bank counterparties. Refer to note 24.

1.7.8 Loans and advances to customers

	2017		2016	
Composition by portfolio - loans and advances to customers	**£m**	**% of book**	£m	% of book
Residential mortgages	16,043	80%	15,964	79%
Non-property SME and corporate	1,371	7%	1,453	7%
Commercial property and construction	652	3%	961	5%
Consumer	2,086	10%	1,709	9%
Loans and advances to customers (before impairment provisions)	**20,152**	**100%**	**20,087**	**100%**
Impairment provisions	(155)		(266)	
Loans and advances to customers (after impairment provisions)	**19,997**		**19,821**	

Gross loans and advances to customers of £20.2 billion increased by £0.1 billion in the year. The key drivers of the movement are primarily as follows:

- residential mortgage lending increased by a net £0.1 billion, with £3.2 billion of new loans originated, offset by repayments on the existing mortgage portfolio of £3.1 billion.
- in the consumer lending portfolio, personal lending increased by £0.2 billion year on year. There was also an increase in Northridge lending of £0.1 billion, and Post Office and AA lending of £0.1 billion; offset by
- a net reduction in the commercial lending portfolio of £0.3 billion. Of this reduction £0.2 billion related to Great Britain Business Banking, which has residual volumes of £0.3 billion at December 2017. Net commercial lending in Northern Ireland decreased, with £0.2 billion of new business in 2017, offset by repayments and redemptions on the existing book of £0.3 billion.

The composition of the Group's loans and advances to customers by portfolio at 31 December 2017 is now 90% residential mortgages and consumer lending based, compared to 88% in 2016.

The growth in the retail lending portfolio reflects the Group's commitment to that market through direct channels, intermediary partners and technological developments.

Specific provisions decreased by 49% to £108 million at 31 December 2017, from £211 million at 31 December 2016 primarily due to the net impact of £137 million of provisions utilised across the portfolios arising from debt management strategies and an impairment charge of £26 million for the year.

Incurred but not reported (IBNR) provisions decreased by 15% to £47 million at 31 December 2017, from £55 million at 31 December 2016, mainly due to improvements in the performance of the commercial loans portfolio.

Further analysis and commentary on changes in the loan portfolios, asset quality and impairment is set out in the Risk Management report, see pages 36 to 55.

1.7.9 Liquid assets

Liquid assets	2017 £m	2016 £m
Balances with central banks	1,806	1,141
Available for sale financial assets	1,008	1,140
Interbank placements	220	210
Total	**3,034**	**2,491**

The liquid assets portfolio comprises Bank of England deposits, available for sale financial assets and bank placements. Available for sale assets can be used to raise liquidity, either by sale, or through secured funding transactions. This portfolio of £3.0 billion increased by £0.5 billion during 2017 reflecting planned balance sheet management activity including participation in the Bank of England Term Funding Scheme (TFS).

At 31 December 2017, the liquid asset portfolio primarily comprised £1.8 billion of Bank of England deposits, £0.4 billion of Multilateral Development Bank bonds, £0.4 billion of UK Government treasury bills, £0.2 billion of covered bonds and £0.2 billion placed with the Parent.

The Group remained in full compliance with the regulatory liquidity regime in the UK throughout 2017 and as at 31 December 2017 maintained a buffer 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, which are disclosed under loans to banks (Refer to note 14).

1.7.10 Customer accounts

Customer accounts	2017 £m	2016 £m
Bank of Ireland UK branded deposits	1,940	2,183
Bank of Ireland UK branded current accounts	2,800	2,513
Post Office branded deposits	13,924	14,567
AA branded deposits	297	212
Total	**18,961**	**19,475**

The Group has a mix of retail and non-retail deposits and current accounts, under Bank of Ireland UK, Post Office and AA brands. The key focus for the Group with respect to its deposit management strategy is to:

- maintain and grow its stable retail customer deposit base;
- prudently manage deposit pricing and margins;
- optimise stable funding levels in line with CRD IV specifications; and
- continue to favourably transform the deposits customer journey.

As at 31 December 2017, the constituent components of customer accounts were retail deposits and current accounts of £15.2 billion, compared to £16.6 billion at 31 December 2016, and non-retail balances of £3.8 billion compared to £2.9 billion at 31 December 2016.

Bank of Ireland UK branded deposits decreased by £0.2 billion in the year and current account balances increased by £0.3 billion, while retail deposit balances originated under the Post Office decreased by £0.6 billion to c.£13.9 billion. Retail deposits originated through the AA partnership increased by £85 million in the year.

The overall reduction in customer account balances of £0.5 billion during 2017 reflects the Group's goal of optimising its overall funding cost (including deposits from banks) and effectively managing its lending growth and overall liquidity position.

1.7.11 Funding

The Group's funding position remains strong at 31 December 2017, with a loan to deposit ratio of 105% (31 December 2016: 102%). The increase in the loan to deposit ratio reflects the net effect of planned increases in consumer lending volumes, primarily in the personal lending portfolio, together with planned decreases in retail deposits due to the efficient management of excess liquidity and drawdowns from the Bank of England TFS.

During 2017 the Group utilised wholesale funding from the Bank of England TFS and Indexed Long - Term Repo (ILTR) scheme, further diversifying the funding base; the TFS provides long term stable funding at rates close to the Bank Base Rate. The Group continues to maintain the operational flexibility to borrow from the market and from other banks including, but not limited to, the Parent.

At present the Group calculates a LCR and a NSFR (which is based on the current draft European Banking Authority (EBA) guidelines) and continues to anticipate buffers above the required levels of 100%.

The Group has a strong funding and liquidity position with a strategy to maintain liquidity risk within risk appetite, at an acceptable cost.

1.7.12 Regulatory capital

Fully loaded CRD IV[1]	2017 £m	2016 £m
Ordinary share capital	851	851
Capital contributions	566	566
Retained earnings and other reserves	215	267
Total equity	**1,632**	**1,684**
Regulatory adjustments	**(124)**	**(132)**
Deferred tax assets relying on future profitability	(73)	(74)
- *Intangible assets*	*(20)*	*(25)*
- *Cashflow hedge reserve*	*(23)*	*(32)*
- *Retirement benefit asset*	*(7)*	*-*
- *Prudent valuation adjustment*	*(1)*	*(1)*
Common equity tier 1 capital	**1,508**	**1,552**
Additional tier 1		
Subordinated perpetual contingent conversion additional tier 1 securities	300	300
Total tier 1 capital	**1,808**	**1,852**
Tier 2		
Dated loan capital	290	335
Total tier 2 capital	**290**	**335**
Total capital	**2,098**	**2,187**
Total risk weighted assets	**10,231**	**10,034**
Capital ratios[2]		
Common equity tier 1 capital ratio	14.7%	15.5%
Tier 1 capital ratio	17.7%	18.4%
Total capital ratio	20.5%	21.8%
Leverage ratio	6.6%	6.9%

Regulatory capital and key capital and leverage ratios

The Group is strongly capitalised with a total capital ratio on a fully loaded basis of 20.5% at 31 December 2017 (31 December 2016: 21.8%).
Total capital resources decreased by £89 million during 2017 to £2.1 billion due to:

- a dividend payment of £160 million paid to the Parent;
- additional tier 1 coupons of £24 million paid to the Parent less a tax credit of £6 million;
- the net repatriation of £45 million of dated loan capital to the Parent (refer to note 29); and
- a decrease in other reserves of £3 million.

offset by:

- profit after tax for 2017 of £129 million; and
- a reduction in regulatory adjustments of £8 million.

RWAs increased from £10.0 billion to £10.2 billion reflecting growth in the consumer portfolios, offset by the impact of the continued deleverage of the Great Britain and Northern Ireland Business Banking portfolio.

IFRS 9 capital impact
The Group has estimated that the quantitative impact from initial adoption of IFRS 9 on 1 January 2018 will reduce the Group's fully loaded CET 1 ratio by c.30 basis points.

The Group has elected to apply the transitional arrangement which, on a regulatory CET 1 basis, will result in minimal impact on initial adoption and which will partially mitigate future impacts in the period to 2022. This will involve a capital addback of a portion of the increase in impairment loss allowance on transition to IFRS 9 and also any subsequent increase in the stage 1 and 2 loss allowances at future reporting dates.

The transition period is for five years, with a 95% addback allowed in 2018, decreasing to 85%, 70%, 50% and 25% in subsequent years.

Leverage
The Group's leverage ratio on a fully loaded basis has decreased by 0.3% to 6.6% at 31 December 2017 which is in excess of the Basel Committee minimum leverage ratio of 3% and the FPC minimum requirement of 3.25%.
The European Commission has proposed the introduction of a binding leverage requirement of 3% as part of the CRD V package proposals. It is anticipated that the binding leverage requirement will be applicable from 2019 at the earliest pending the final agreement of the proposals at EU level.

The following tables provide year on year analysis of the movements in the leverage exposure, tier 1 capital and the leverage ratio.

[1] *Capital figures disclosed reflect the consolidated UK regulatory position for the BoI UK regulatory group which consists of the Bank and NIIB Group Limited only.*
[2] *Capital ratios have been presented including the benefit of the retained profit in the period in accordance with Article 26 (2) of the Capital Requirements Regulation (CRR).*

1.7.12 Regulatory capital (continued)

Fully loaded CRD IV	2017 £m	2016 £m
Total assets	**26,235**	**25,960**
Removal of accounting value of derivatives and securities financing transactions (SFTs)	(27)	(55)
Removal of accounting value of the assets of unregulated entities	(78)	(68)
On balance sheet items (excluding derivatives and SFTs)	**26,130**	**25,837**
Exposure value for derivatives and SFTs	177	97
Off balance sheet items post application of credit conversion factors	605	502
Other adjustments	348	549
Total leverage ratio exposures	**27,260**	**26,985**
Tier 1 capital	**1,808**	**1,852**
Leverage ratio[1]	**6.6%**	**6.9%**

Pillar 1 capital requirements	2017 Capital required[1] £m	2017 RWA £m	2017 Net value of Exposure[2] £m	2016 Capital required[2] £m	2016 RWA £m	2016 Exposure £m
Central governments or central banks	1	13	3,636	1	19	2,975
Public sector entities	-	-	15	-	-	16
Multinational development banks	-	-	394	-	-	356
Institutions	3	44	2,058	6	69	2,965
Corporates	107	1,334	1,992	117	1,461	2,153
Retail	149	1,861	5,342	114	1,424	4,555
Secured by mortgages on residential property	442	5,525	16,528	449	5,623	16,257
Exposures in default	31	382	345	33	410	371
Covered bonds	3	35	175	3	37	187
Equity	4	44	44	-	2	2
Other items	18	237	421	17	210	345
Credit and counterparty risk	**758**	**9,475**	**30,950**	**740**	**9,255**	**30,182**
Operational risk	60	756	-	62	779	-
Total	**818**	**10,231**	**30,950**	**802**	**10,034**	**30,182**

1 Capital required is 8% of the RWAs.
2 The net value of exposures includes gross balance sheet amounts and off balance sheet commitments net of provisions.

1.7.12 Regulatory capital (continued)

Movement in regulatory capital - Fully loaded - CRD IV	2017 £m	2016 £m
Opening common equity tier 1 capital	**1,552**	**1,612**
Contribution to common equity tier 1 capital from profit	129	163
Dividends and coupons paid to the Parent, net of tax	(178)	(239)
Net actuarial gain / (loss) on defined benefit schemes	6	(3)
Other reserves	(10)	24
	1,499	1,557
Regulatory adjustments	**9**	**(5)**
- Deferred tax relying on future profitability	*1*	*10*
- Intangible assets	*5*	*5*
- Cashflow hedge reserve	*9*	*(21)*
- Retirement benefit asset	*(7)*	*2*
- Prudent valuation adjustment	*1*	*(1)*
- Qualifying holdings outside of the financial sector	*-*	*-*
Closing common equity tier 1 capital	**1,508**	**1,552**
Opening additional tier 1 capital	**300**	**300**
Closing additional tier 1 capital	**300**	**300**
Total tier 1 capital	**1,808**	**1,852**
Opening tier 2 capital	**335**	**335**
Dated loan capital repurchased	(135)	-
Dated loan capital issued	90	-
Closing tier 2 capital	**290**	**335**
Closing total regulatory capital	**2,098**	**2,187**

Regulatory capital to statutory total equity reconciliation - Fully loaded CRD IV	2017 £m	2016 £m
Regulatory total tier 1 capital	1,808	1,852
Consolidation of jointly controlled entity (note 18)	61	61
Consolidation of subsidiary undertakings	6	5
Reverse regulatory adjustments to capital:		
Deferred tax assets relying on future profitability	73	74
Intangible assets	20	25
Cashflow hedge reserve	23	32
Retirement benefit asset	7	-
Prudent valuation adjustment	1	1
Statutory total equity	**1,999**	**2,050**

1.7.13 Segmental performance

Consolidated income statement - profit / (loss) before taxation	2017 £m	2016 £m
Great Britain Consumer Banking	134	165
Northern Ireland	53	50
Great Britain Business Banking	12	15
Group Centre	(48)	(37)
Profit before taxation	**151**	**193**

2017 has been a year of solid performance against the backdrop of wider economic and political uncertainties and ongoing competitive market conditions.

The Group has continued to invest in new product propositions in order to position it favourably for future growth.

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

Great Britain Consumer Banking
Great Britain Consumer Banking profits decreased by £31 million to £134 million in 2017, primarily due to:

- lower income recognised on its acquired mortgage portfolio given stronger loan retention on certain products than initally expected;
- increasing competitive margin and mix pressures in the mortgage and cards business; offset by;
- significant year on year reductions in retail funding costs; and
- strong performance on personal loan volumes.

Consumer new business lending volumes increased to £4.4 billion, an increase of £0.5 billion on 2016.

Great Britain Consumer Banking impairment charges increased modestly by £10 million given the planned growth in the consumer lending portfolios.

Great Britain Consumer Banking gross lending volumes increased to £18.1 billion.

Northern Ireland
The Northern Ireland results include the Bank of Ireland branch network and business centres, personal lending, Bank of Ireland credit cards and mortgages, and the banknote issue business. Profits in Northern Ireland have increased by £3 million reflecting a strong net margin performance and ongoing cost management.

The commercial lending portfolio in Northern Ireland decreased by £0.1 billion to £1.3 billion at 31 December 2017 due to provision utilisation and repayments in excess of new lending.

Great Britain Business Banking
This business primarily includes the commercial lending portfolio which is undergoing a continued process of managed deleveraging and decreased by £0.2 billion during the year to £0.3 billion at 31 December 2017. Profits have decreased by £3 million, mainly due to reduced lending income and movements in impairment charges.

Group Centre
The Group's funding, liquidity and capital position are managed centrally, and the related costs are reported under this segment, along with staff and operating costs of the central risk and control functions and regulatory related costs.

The loss in this segment has increased by £11 million, due to increased operating expenses which largely relate to continued investment in products, regulatory change, staffing and IT systems.

1.8 Principal risks and uncertainties

Principal risks	Outlook	Potential risk impact	Key controls and mitigating factors
Credit risk 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, country risk, credit concentration risk and settlement risk.	**Stable** Credit conditions are expected to remain stable. However, macroeconomic uncertainty continues as a result of the outcome of the UK referendum on EU membership that has the potential to impact credit risk.	Should commercial or consumer customers be unable to meet their obligations in relation to borrowings from the Group, the Group may suffer increased losses and this would have an adverse impact on the Group's financial position.	• A Risk Appetite Framework is in place and aligned with the Group's overall strategy; • Leveraging of detailed macro-economic data, providing granular insight on geographic exposures and housing market movements on a quarterly basis to CRPC; • External Mortgage Indemnity Guarantee for loans >90% LTV, providing protection against future loss occurrence; • Underlying lending policies are aligned to risk appetite; • Exposure to excessive credit losses is minimised through the operation of responsible lending practices and active portfolio management within clearly defined Board approved risk appetite limits; • The Group undertakes active credit management to maximise recoveries from impaired assets seeking the best outcome in accordance with the Group's Customer Charter; • Active management of credit risk concentrations is an integral part of the Group's approach with the risk appetite statement specifying a range of exposure limits for credit risk concentration over the planning period; • Regular monitoring of lending portfolios by senior management and the Credit Risk Portfolio Committee (CRPC). For selected portfolios, this also includes the review of stress scenarios at the Executive Risk Committee (ERC), Board Risk Committee (BRC) and the Board; and • At least annual reviews of all commercial portfolio cases to monitor case specific risk.
Liquidity and funding risk 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. Funding risk is the risk that the Group does not have sufficiently stable and diverse sources of funding or has an inefficient funding structure.	**Stable** The Group maintains a portfolio of unencumbered liquid resources in excess of regulatory and internal requirements. The Group successfully gathered deposits during the year through the Post Office, the AA and the NI business. The Group also successfully borrowed funds from the Bank of England and the Parent during the year.	The Group is primarily funded by way of retail deposits, therefore a 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. This in turn would have a materially adverse effect on the Group's results, financial condition and liquidity position. A loss of confidence in the economy generally, the financial services industry, the Post Office brand, the AA brand or the Group or the Parent specifically, could lead to a reduction in the Group's ability to access customer deposit funding on appropriate terms.	• A liquidity and funding Risk Management Framework (RMF) which is reviewed annually, is in place and is aligned with the Group's overall strategy to be a self-funded business with no material funding dependency on the Parent or the wholesale funding market. The Liquidity and Funding Risk policy which governs management and monitoring, sits within this framework; • Daily monitoring and management of the liquidity position including, but not limited to, regulatory and internal liquidity stress testing, early warning signals, metrics and a defined escalation process; • Regular reporting to the Asset and Liability Committee (ALCo), the ERC, the BRC and the Board; • Maintenance of unencumbered liquidity resources 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 and contingent liquidity collateral; • 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 to determine the amount of ongoing new retail deposit acquisition and retention required to fund the Group's asset base; • Comprehensive Internal Liquidity Adequacy Assessment Process (ILAAP) undertaken annually which sets out how the Group assesses, quantifies and manages key liquidity and funding risks; and • Recovery Plan in place, which specifies a range of processes and potential actions that can be put in place enacted, in the event of any unexpected shortfall in liquidity and / or funding.

1.8 Principal risks and uncertainties (continued)

Principal risks	Outlook	Potential risk impact	Key controls and mitigating factors
Market risk The risk of loss arising from movements in interest rates, FX rates or other market prices. Market risk arises from the structure of the balance sheet, the Group's business mix and discretionary risk taking. Market risk can also arise where variable rate assets and liabilities reprice at different frequencies, or where lending reprices with changes in central bank rates but is funded at short dated market rates.	**Stable** The Group continues to manage interest rate and foreign exchange exposure to acceptable levels by seeking natural hedge solutions within the balance sheet and by hedging residual exposures with the Parent as the hedge counterparty.	The effective management of market risk is essential to the maintenance of stable earnings, the preservation of capital resources and the achievement of the Group's strategic objectives. Changes in the basis between different reference rates (such as assets repricing at base rate and liabilities repricing at London Interbank Offered Rate (LIBOR)) may have an adverse impact on the Group's net interest margin and profitability.	• A market risk management framework which is reviewed annually, is in place and aligned with the Group's overall strategy to have no risk appetite for discretionary market risk and minimise its exposure to market risks in relation to Interest Rate Risk in the Banking Book (IRRBB) and FX. The market risk policy, which governs market risk management and monitoring, sits within this framework. • The Group's market risk is mitigated through hedging with the Parent, using derivatives or cash hedging deals; • A product approval process incorporates review of product terms and conditions from a market risk perspective, to ensure compliance with existing risk appetite, policy, and process. • Regular reporting to the ALCo, the ERC, the BRC and the Board; and • Daily market risk stress tests across all aspects of market risk (yield curve and repricing risk, basis risk, prepayment risk, pipeline risk etc.) are produced and monitored against red, amber and green (RAG) limits set by Board and operational thresholds set by the ALCo.
Regulatory risk The risk of failure to meet new or existing regulatory and / or legislative requirements and deadlines or to embed requirements into processes.	**Risk Increasing** Further details of evolving regulatory and legislative requirements are set out in section 1.9.	The increasing regulatory agenda necessitates an increase in resources and amendments to current processes which may impact the Group's cost base. Failure to comply with all aspects of the relevant regulatory regimes could result in the Group being subject to fines, customer compensation and / or the requirement to pay regulatory sanctions and harm its reputation.	• The Group has no appetite for failure to comply with its regulatory or legislative obligations; • Regular and open communication with the FCA, PRA and Single Supervisory Mechanism (SSM) on all aspects of the Group's activities; • Regular reporting to senior management, the Regulatory and Operational Risk Committee (R&ORC), the ERC, the Executive Complaints Oversight Forum (ECOF), the BRC and the Board; • Regular monitoring, assessment and reporting of regulatory change (current and proposed) to ensure timely and appropriate response to regulatory change requirements at both a UK and EU level; • Risk-based regulatory and compliance monitoring performed by independent compliance monitoring functions; and • Embedding of risk culture through the Risk Management Framework (RMF).

1.8 Principal risks and uncertainties (continued)

Principal risks	Outlook	Potential risk impact	Key controls and mitigating factors
Operational risk and Financial crime Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. Principal operational risks include Information Technology and Security (including Cyber risks), Business Disruption, Financial Crime (incorporating the risk of facilitating money laundering, terrorist financing, sanctions violation, and fraud), Sourcing, Legal, Model and People Risk, but exclude Strategic and Reputational risk.	**Risk increasing** Along with other financial service providers, the Group is reliant on IT systems to deliver products and services. Increasing risk of failure of IT systems and external threats such as cybercrime or material fraud events, could lead to disruption of services for customers, financial loss and / or reputational damage. Increasing legislative and regulatory requirements in relation to money laundering, terrorist financing and sanctions violation are ongoing areas of focus for the Group. A significant number of Group services and processes are provided by the Parent and third parties and failure of a material outsourced service provider remains a key operational risk.	The Group is exposed to a broad range of operational risks as a consequence of conducting its day-to-day business activities. Such risks include the availability, resilience, stability and security of core IT systems (including those protecting the Group from cybercrime); the continuity of the Group's operations and services; the risk of the Group's products and services being used to commit financial crime; risks arising from Sourcing arrangements and Legal and People Risk. Cybercrime remains an evolving threat to the Group and its strategic objectives. Increased digital interconnectivity across the Group, its customers and suppliers has the potential to heighten vulnerability to cyber-attacks, which could disrupt service for customers, and cause financial loss and reputational damage. The regulatory change landscape continues to absorb resource. Non-compliance with legislative and regulatory obligations may result in financial penalties, regulatory reprimand and reputational risk to the Group. Litigation proceedings with adverse judgments could result in restrictions or limitations on the Group's operations or result in a materially adverse impact on the Group's reputation or financial condition. Management stretch gives rise to the potential risk of loss of key staff.	• The Group's operational risk management framework (ORMF) defines the Group's approach to identifying, assessing, managing, monitoring and reporting on the operational risks that may impact the achievement of the Group's objectives. The ORMF consists of processes and standards aimed at embedding adequate and effective risk management practices within business units throughout the Group; • The Group Risk Appetite incorporates Operational risk appetite statements and limits as approved by the Board; • The Group utilises a number of available strategies in controlling its exposure to operational risk, with the primary strategy being the maintenance of an effective control environment, coupled with appropriate management actions; • Specific policies and risk mitigation measures for material operational risks are in place; • The Group continues to enhance and invest in its risk management processes including the identification of and controls for potentially elevated / emerging risks such as, Information Technology, Information Security and Cybercrime, Business Disruption, Financial Crime and Fraud. This enhancement and investment is intended to, over time, improve the Group's risk profile; • Security programmes are in place to protect the integrity and availability of the Group's systems and mitigate the frequency and impacts of cyber-attacks; • A staff education programme has been implemented on information protection and cyber security; • A Group wide programme is underway to enhance the maturity levels of the anti-money laundering (AML) risk management framework, including automation; • Arrangements entered into with the Parent and third party outsourced providers are governed through service level agreements, service descriptions and KPIs which are formally monitored. This has been and continues to be further enhanced; • The Group has processes in place to ensure its compliance with its legal obligations, together with clear controls in respect of the management and mitigation of such disputes, proceedings and investigations as may be instigated against the Group from time to time; • The Group has a Board approved people strategy to enable the Group to retain appropriate numbers and / or calibre of staff having regard to remuneration restrictions imposed by government, tax or regulatory authorities. These include Talent Board Reviews including succession planning, a Performance Management Framework, and a Career and Reward Framework; and • Regular reporting to the R&ORC, the ERC, the BRC and the Board.

1.8 Principal risks and uncertainties (continued)

Principal risks	Outlook	Potential risk impact	Key controls and mitigating factors
Business / Strategic risk The risk of volatility to the Group's projected outcomes, including the Income Statement and Balance Sheet impact and / or damage to its franchise including that of the Group's joint ventures. It includes volatilities caused by changes in the competitive environment, new market entrants, new products or failure to develop and execute a strategy, or anticipate or mitigate a related risk. This includes pricing, partner appetite, customer confidence and credit demand, collateral values and customers' ability to meet their financial obligations and consequently adversely impact the Group's financial performance, balance sheet and capital. Other effects may include further changes in interest rates, which can impact the Group's revenues. Brexit: Uncertainty following the UK vote to exit the EU - particularly relating to the nature and impact of withdrawal - could affect the environment in which the Group operates.	**Stable yet uncertain** The competitive environment in which the Group operates remains challenging and macroeconomic uncertainty continues as a result of the ongoing negotiations regarding the UK's withdrawal from the EU.	Adverse change in the Group's revenues and / or costs resulting in reduced profitability.	• A clearly defined strategic plan is developed within the boundaries of the Board approved risk appetite and risk identity, ensuring balanced growth in consumer lending and deposits with a stable funding profile that is appropriate for the asset mix; • The Group's Annual Strategy & Planning Process includes a review and assessment of the Group's Business Model; • The Group monitors the impact, risks and opportunities of changing current and forecast macroeconomic conditions on the likely achievement of its strategy and objectives. This is supported by the Group's Economist and supplemented with external research as required; • Macroeconomic tools allied to the Group's credit risk appetite mitigate the impacts associated with a severe house price correction; • Competitive environment reviewed and monitored on an ongoing basis to identify market developments; • Expert independent validation of key strategic items and / or developments; • Specific business focus on new lending origination, deposit sales and active customer retention to ensure a balanced portfolio and appropriate funding base; • Clearly defined and regularly monitored KPIs at both Executive and Board committee level; • Active engagement and management of the Post Office, the AA and other relationships; • In the context of its Board approved strategy, the Group assesses and develops its complementary technology strategy which is reviewed and monitored on an ongoing basis; • The Group is strongly capitalised and self-funded predominantly through retail deposits with no sustained funding dependency on the parent or material dependency on the wholesale funding market. The Group also has significant liquidity collateral which is capable of being pledged against borrowings from central banks or other external market participants; • The Group conducts business in the UK through key partnerships which reduces the Group's investment in infrastructure and other items of a fixed cost nature; • The Group market risk exposure is managed tightly and is substantially eliminated through hedging with the Parent. The Group has no appetite for market risk; and • Regular reporting to the ERC, the BRC and the Board.

1.8 Principal risks and uncertainties (continued)

Principal risks	Outlook	Potential risk impact	Key controls and mitigating factors
Reputation risk The risk to earnings or franchise value arising from adverse perception of the Group's image on the part of customers, suppliers, counterparties, shareholders, staff, partners, legislators or regulators. This risk typically manifests through a loss of business in the areas affected.	**Stable** 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 strategic partners and / or keep and attract customers. Ultimately this may result in an adverse impact on the Group's business, financial condition and prospects.	• The embedding and management of a positive customer conduct culture to ensure the interests of consumers remain at the heart of the Group's operation. Management decision making aims to deliver an accurate, open and positive external view of the Group to customers, regulators and the wider public and community; • Active management of all internal and external communications including social media; • Maintenance of a suite of early warning indicators, which, if breached, will trigger escalation and, where required, management action; • Regular reporting to the ERC, the BRC and the Board; and • Regular and open dialogue with key stakeholders, partners, regulators and industry bodies.
Capital adequacy risk The risk that the Group holds insufficient capital to absorb extreme and unexpected losses, which could eventually result in insolvency.	**Stable** The Group continues to generate capital and maintains a strong capital position against regulatory and internal requirements.	The Group's capital ratios would deteriorate relative to regulatory requirements as a result of materially worse than expected financial performance or unexpected increase in risk weighted assets.	• A capital management framework which is reviewed annually, is in place for the effective management of capital adequacy risk and its capital position. The capital management policy, which governs capital management and monitoring, sits within this framework. • Comprehensive Internal Capital Adequacy Assessment Process (ICAAP) undertaken annually, assessing the Group's capital adequacy and capital quality under plausible stress scenarios; • Capital adequacy risk appetite is central to the strategic planning process. The Group's appetite is to hold sufficient capital to achieve its strategic objectives, as well as to absorb extreme losses in a stress scenario; • Regular reporting to the ALCo, the ERC, the BRC and the Board; • Detailed capital plan continuously monitored and reviewed on a monthly basis, which informs the capital position for the Group; and • Recovery plan in place which specifies a range of processes and potential actions that can be enacted in the event of any unexpected shortfall in capital resources.

1.8 Principal risks and uncertainties (continued)

Principal risks	Outlook	Potential risk impact	Key controls and mitigating factors
Conduct Risk Conduct risk is the risk of failure to deliver a product or service in a manner promised or reasonably expected by customers.	**Stable** Scoping and provisioning in respect of the Plevin PPI ruling has been completed, with customer management and resolution in place for 2018. No other immediate threats to a stable environment based on known external, economic or regulatory focus are anticipated.	Conduct risk and / or poor outcomes for customers could lead to customer remediation, loss of business, adverse media coverage, financial penalties and / or regulatory sanction.	• The Group has no appetite for customer detriment and seeks to be fair, accessible and transparent in the provision of products and services to its customers; • The Group has developed an internal Customer Charter which provides a clear articulation of its customer and partner commitments and is designed to place customers at the heart of its business. It is central to the Group's Conduct Risk Culture which continues to be embedded across the business and provides a common and consistent framework for business decision making and product design across the Group; • The Product & Services Approvals & Governance Committee (PSAGC) reviews, assesses and approves material new products and services prior to introduction or withdrawal or material change to an existing product or service. It also reviews the performance of existing products and services to ensure these remain appropriate; • Conduct measures throughout the Group include enhanced product review process, Complaint Root Cause Analysis and Conduct Risk MI; and • Regular reporting to the R&ORC, the ERC, the BRC and the Board.

Impact of Accounting Standards
IFRS 9 is an accounting standard which became effective on 1 January 2018. Its forward-looking 'expected credit loss' (ECL) approach resulted in higher impairment provisions on transition to IFRS 9 and may lead to more volatile impairment charges with a consequent impact on capital ratios.

Key mitigating considerations:

- The estimated initial impact of IFRS 9 on capital has been incorporated into the Group's capital planning and the Group retains sufficient buffers in excess of regulatory requirements on a fully loaded basis. The Group is availing of the transition arrangements for mitigating the impact of IFRS 9 on regulatory capital. These arrangements include relief for a proportion of any increase in stage 1 and 2 loss allowances between transition and the relevant reporting date.

- Further detail in relation to IFRS 9 is set out in the credit risk section of the Risk Management Report on pages 53 to 55.

The Strategic report on pages 5 to 29 is approved by the Board of Directors and signed on its behalf by:

Thomas McAreavey

Thomas McAreavey
Director
6 March 2018
Company number: 07022885

Risk Management

The information below in sections or paragraphs denoted as audited in sections 2 and 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 85.

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 follows an integrated approach to risk management to ensure that all material classes of risk are taken into consideration and that the Group's overall business strategy and remuneration practices are aligned with its risk strategy and capital plan.

The Group's RMF articulates this integrated approach and is approved by the Board of Directors (the Board) on the recommendation of the BRC on a periodic basis. It describes the Group's risk categories, risk governance structure and process, framework for setting risk appetite and its approach to risk identification, measurement, management and reporting.

The RMF is underpinned by an appropriate risk culture and is enabled by people, processes and technology. In the RMF the Group categorises and defines the risks faced by the business. This categorisation supports the Group's risk management activities at all levels and enables risks to be clearly and consistently identified, assessed, managed and reported to key stakeholders. These categories are subject to ongoing review and maintenance to ensure they remain appropriate in the context of a changing strategic and business environment.

The Group's principal risks and uncertainties are set out in section 1.8 of the Strategic report. The component elements of the RMF are outlined in the chart below.

Figure 1 - Bank of Ireland UK Risk Management Framework components

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.

1.1 Risk governance framework

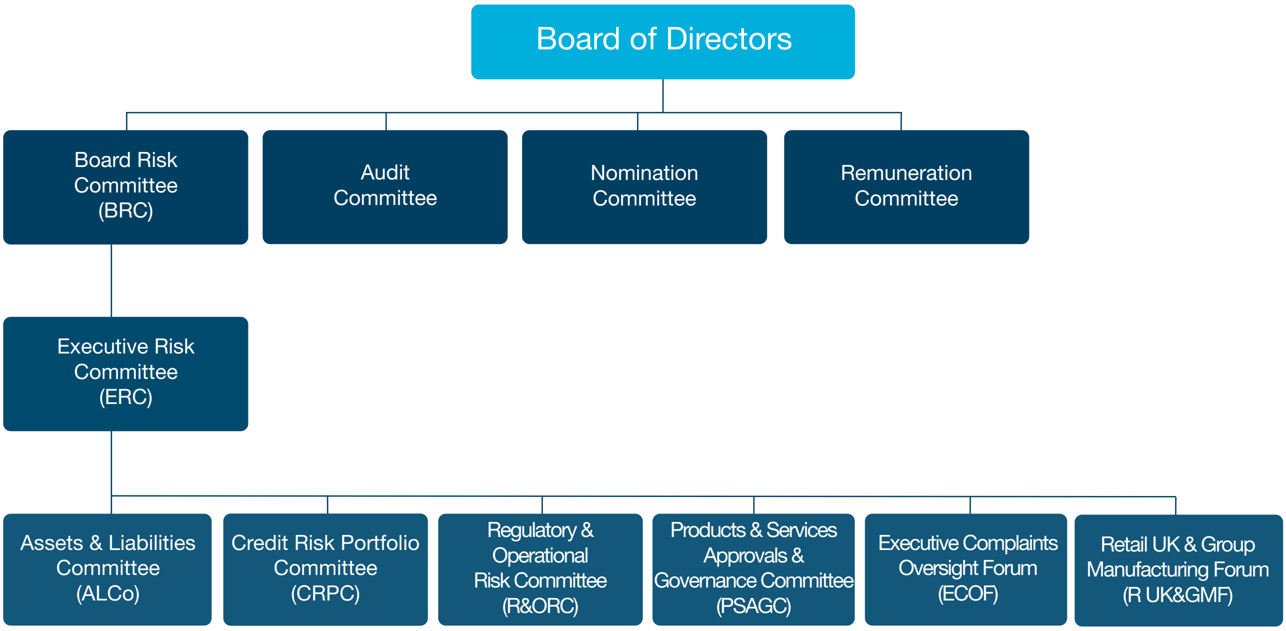
1.1.1 Roles and responsibilities – Bank of Ireland UK Board and Executive Governance

The Group's organisational structure is designed to facilitate the reporting of risk positions and escalation of risk concerns from business units, functions and Group Internal Audit (GIA) to the ERC, the BRC and the Board, and to cascade approved risk management policies to the business units.

The Board is responsible for ensuring that an appropriate risk strategy and system of internal control is maintained and for reviewing its effectiveness. To assist the Board in discharging its duties, it has appointed four Board sub-committees.

Below this Board level governance, the Group also has in place a suite of executive level committees (as shown in figure 2 below).

Figure 2 – Risk Committee Governance Structure



Each of the risk committees detailed in figure 2 has detailed terms of reference, approved by its parent committee or the Board, setting out its objectives and responsibilities. In summary, the following are the key responsibilities of the Group's Board and its sub-committees:

Board of Directors
The Board is responsible for approving policy and strategic direction in relation to the nature and scale of risk that the Group is prepared to assume, to achieve its strategic objectives. The Board ensures that an appropriate system of internal control is maintained and reviews its ongoing effectiveness. The Board approves the Group's risk appetite.

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

Board Risk Committee
The BRC is responsible for monitoring risk governance, and assists the Board in discharging its responsibilities in ensuring that risks are properly identified, reported, and assessed; that risks are properly controlled; and that strategy is cognisant of the Group's risk appetite within the overall risk appetite of its Parent.

The BRC meets at least four times a year and more frequently if required, and its membership is made up of at least three independent non-executive Directors.

Audit Committee
The Audit Committee is responsible for the appropriateness and completeness of the Group's system of internal control and ensuring this is adequately resourced; advising the Board (in close liaison with the BRC) in relation to the setting of standards for the Group's risk control framework; reviewing the manner and framework in which management ensures / monitors the adequacy of the nature, extent and effectiveness of internal control systems (including accounting control systems); monitoring the integrity of the financial statements and financial reporting process; overseeing all matters relating to the relationship between the Group and its External Auditors; and monitoring the effectiveness of its Parent's Internal Audit's functions and operations as they relate to the Group.

The Audit Committee meets at least four times a year and more frequently if required, and its membership is made up of at least two independent non-executive Directors.

1.1.1 Roles and responsibilities – Bank of Ireland UK Board and Executive Governance (continued)

Nomination Committee
The Nomination Committee is responsible for leading the process for appointments and renewals for the Board and the Board Committees as appropriate, and making recommendations in this regard to the Board for its approval, reviewing succession plans for and approval of the senior management team and regulatory Senior Management Function appointments.

The Nomination Committee meets at least twice a year and more frequently if required, and its membership is made up of three non-executive Directors.

Remuneration Committee
The Remuneration Committee is responsible for considering the remuneration policy for Directors, senior management and top earners in the Group. It is responsible for ensuring that the Group operates remuneration policies and practices which are in line with the principles of the EU Capital Requirements Directive and any associated guidance from the EBA, the FCA and the PRA, as to its application.

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

Executive Risk Committee
The ERC is the most senior executive risk committee and reports directly to the BRC. Membership comprises the Chief Executive Officer (CEO), Chief Financial Officer (CFO), Chief Risk Officer (CRO), Chief Operating Officer (COO), Director of Human Resources (HR), Heads of Business and Senior Risk Managers. It is responsible for the end to end management of risk across the Group including monitoring and reviewing the Group's risk profile and compliance with risk appetite. It approves risk policies in accordance with the mandate delegated by the BRC. The ERC Terms of Reference are approved by the BRC.

The ERC in turn delegates specific oversight of the major classes of risk to specific committees that are accountable to it. These committees are:

- **Asset & Liability Committee** - responsible for ongoing review and monitoring of balance sheet, liquidity, funding, market risk and capital positions in order to ensure compliance with relevant Group RAS limits, regulatory requirements and industry best practice.
- **Credit Risk Portfolio Committee** - responsible for overseeing the Group's development, deployment and management of the Credit Risk framework and corresponding risk appetite across all asset classes.
- **Regulatory & Operational Risk Committee** - responsible for the end-to-end management and oversight of Regulatory, Operational, Financial Crime and Conduct Risks within the Group.
- **Products & Services Approvals & Governance Committee** - reviews, assesses and approves material new products and services across the UK prior to introduction or prior to withdrawal or material changes to an existing product / service. It also considers the performance of existing products and services to ensure they remain fit for purpose.
- **Executive Complaints Oversight Forum** - responsible for the end-to-end oversight of complaints and associated activity. It oversees the approach to management of complaints and drives improvements to this approach through challenge and a focus on continuous improvement.

The ERC approves the terms of reference and the membership of its appointed committees annually, reviews their decisions and minutes and reviews the findings of the annual effectiveness reviews of the committees.

1.1.2 Roles and responsibilities – Three Lines of Defence

The Group has adopted the 'three lines of defence' model as the basis for its RMF, as indicated below:

Figure 3 – Three Lines of Defence model

1.1.2 Roles and responsibilities – Three Lines of Defence (continued)

First line of defence – Primary responsibility and accountability for risk management lies with line management across the business and front-line functions. They are responsible for the identification and management of risk against risk appetite at a business unit level including the implementation of appropriate controls and the reporting of all major risk events. Business units are accountable for the risks arising in their businesses / functions, and are the first line of defence for the Group in managing these. This applies irrespective of whether or not activities are outsourced to the Parent or to external third parties including strategic partners such as the Post Office and the AA.

In addition, the Group's treasury function is responsible for liquidity planning and management, transfer pricing, balance sheet management, cash and market risk management and as part of the Group's Recovery Plan, contingent capital and funding management actions. The UK Treasurer reports directly to the CFO.

Second line of defence – The Second Line Risk Function is responsible for maintaining independent risk oversight and ensuring that a risk control framework is in place.

In order for the BRC, the ERC, and other risk committees to fulfil their delegated responsibilities in respect of risk governance, they are supported by the Risk Function which is responsible for establishing the RMF and designing risk policies and communicating these to all business units. The Risk Function also provides independent oversight, monitoring, analysis and reporting of key risks. This includes the monitoring and credit underwriting of individually significant credit exposures in the commercial loan book.

Third line of defence – The Internal Audit function provides independent and reasonable assurance to key stakeholders on the effectiveness of the Group's risk management and internal control framework. GIA carries out risk based assignments covering Group businesses and functions (including outsourcing providers), with ratings assigned as appropriate. Findings are communicated to senior management and other key stakeholders, with remediation plans monitored for progress against agreed completion dates. The Group Credit Review (GCR) function, an independent function within Internal Audit, is responsible for reviewing the quality and management of credit risk assets across the Group.

1.2 Risk culture, strategy and principles

Risk culture
A strong risk culture is fundamental to the Group's management, with the Group's Risk Culture Statement being approved by the Board. The Group promotes a risk culture that is open and risk aware. Considerations about risk inform the Board, day-to-day management decision-making and product development. Clearly defined roles and responsibilities ensure risk is owned and controlled effectively across the organisation. A Speak Up policy protects employees who wish to speak out.

Risk strategy
The Group's Risk Strategy is to protect its balance sheet, customers and reputation as well as those of its strategic partners, and help the business to build profitability. The Group seeks to accomplish this by:
- establishing Risk Appetite as the boundary condition for the Group's Strategic Plan and Annual Operating Plan / Budget;
- defining and implementing a Risk Management Framework to manage risk in an integrated approach;
- defining Risk Principles upon which risks may be accepted;
- allocating clear roles and responsibilities / accountability for the control of risk within the Group; and
- engendering a prudent risk management culture.

Risk principles
Risk Owners seeking to accept a risk at transaction, portfolio and Group level must operate in accordance with risk frameworks and policies including bringing this to the attention of the ERC where required.

In general, risks may be accepted if:
- they are aligned with the Risk Identity and within Risk Appetite
- the risks represent an attractive investment from a risk-return perspective. It is imperative that investment decisions achieve a return on capital which are in excess of the pre-defined hurdle rates and also managed within formally approved mandates. There are a number of return on capital metrics currently in use by the Group at a product level, namely the BoI Group Risk Adjusted Return on Capital (RAROC), Return on Equity (ROE) and Return on Regulatory Capital (R&ORC). At an entity level, the Group also use a ROE measure which is based on the firm's statutory balance sheet.
- the Group has the resources and skills to analyse and manage the risks;
- stress and scenario tests around the risks exist, where appropriate, and results are satisfactory;
- appropriate risk assessment, governance and procedures have been observed as described in the appropriate documentation (e.g. frameworks, policies, processes, controls) pertaining to individual risk categories or at an aggregate Group-level; and
- acceptance of the risk does not cause undue risk concentration in order to remain within the approved Risk Appetite portfolio limits and not deviate from the Risk Identity.

1.3 Risk identity and risk appetite

Risk identity
The Group's purpose is to be the leading partnership bank, providing simple, flexible, relevant, accessible financial services and products to UK customers both directly and through partnerships with trusted, respected UK brands and intermediaries, thereby providing attractive sustainable returns to our shareholder.

To achieve its Risk Strategy, the Group operates a strong risk management framework and risk culture whilst pursuing an appropriate return to the risk taken.

Risk appetite
Risk appetite defines the amount and nature of risk that the Group is prepared to accept in pursuit of its strategic objectives. It is central to the strategic planning process, forms a boundary condition to strategy and guides the Group in its risk-taking and related business activities. The Risk Appetite Statement (RAS) is defined in accordance with the Group's RMF and is reviewed at least annually by the Risk Office and approved by the Board on the recommendation of the BRC.

Risk appetite is defined in qualitative and quantitative terms within a framework that facilitates discussion and monitoring both at the Board and management levels. At the highest level, risk appetite is based on the Group's risk identity, which qualitatively defines the relative positioning of the Group's activities within a spectrum of business models and market opportunities. Quantitative risk appetite measures, which are consistent with the Group's risk identity, are then used to inform the boundaries of the Group's strategy. These measures also inform individual risk limits and targets at management and business unit level.

The Group tracks actual and forecast results against these risk limits which are monitored and reported regularly to senior management as well as the ERC sub-committees; the ERC; the BRC and the Board.

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 pages 24 to 29 within the Strategic report.

Where risk appetite is breached or an unanticipated risk arises, a root cause analysis will be undertaken by the designated risk owner.

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 considered material are included in the Group's RMF, owners are identified, appropriate policies are put in place, and a formalised measurement and management process is defined and implemented. The Group periodically reviews the RMF 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, liquidity and on its ability to trade in the future and these are covered in the principal risks and uncertainties that are set out on pages 24 to 29 of the Strategic report.

Risk measurement
Risk management systems are in place to facilitate measurement, monitoring and analysis of risk 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 the BRC and the Board as an integral part of the ICAAP and the ILAAP, 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 as well as appropriate controls and mitigants.

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. The CEO and CRO reports submitted to each Board meeting provide an update on key risk issues as well as an update on performance against core risk appetite metrics. Additionally, material risks identified under the Group's RMF are assessed and their status is reported in the Monthly Risk Report (MRR) in the first instance. This report is submitted to both the ERC and the BRC.

The format of this report is approved by the BRC. The content of the MRR 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 MRR, the BRC and the Board consider more frequent formal updates on other key risk areas.

Data on the external economic environment and management's view of the implications of this environment on the Group's risk profile is also reviewed regularly at management and Board level. The BRC also receives risk information through the review of minutes from the ERC.

Risk Improvement Roadmap (RIR)
Under the management of the CEO and the CRO, a RIR was designed to continue to build on work undertaken to embed a strong risk management framework and risk culture in 2017. Following implementation, the RIR transitioned to business as usual, under the Risk Management Framework, at year end.

2 Management of key risks

2.1 Credit risk

Key points:

- Gross loans and advances to customers increased by £0.1 billion to £20.2 billion at 31 December 2017 (31 December 2016: £20.1 billion).
- The commercial property sector continues to improve, but in some segments, such as Northern Ireland's land and development sector, it continues to be characterised by low levels of activity and relatively illiquid markets.
- Total impairment charges have increased from £23 million for 2016 to £26 million for 2017, driven by maturity in assets originated in the Personal Loan book since 2015.
- The residential mortgage portfolio has continued to perform well. Arrears and default rate performance continues to be ahead of expectations.
- All lending portfolios have performed ahead of impairment expectations.

2.1.1 Definition of credit risk

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. This risk comprises country risk, default risk, recovery risk, exposure risk, the credit risk in securitisation, cross border (or transfer) risk, concentration risk and settlement risk. At portfolio level, credit risk is assessed in relation to the degree of name, sector and geographic concentration to inform the setting of appropriate risk mitigation and transfer mechanisms and to assess risk capital requirements. The manner in which the Group's exposure to credit risk arises, its policies and processes for managing it, and the methods used to measure and monitor it, are set out below.

How credit risk arises
Credit risk arises from loans and advances to customers. It also arises from the financial transactions the Group enters into with financial institutions, sovereigns and state institutions. It comprises both drawn exposures and exposures the Group has committed to extend. While the Group could potentially suffer loss to an amount equivalent to its undrawn commitments, the Group does not expect to incur losses to that extent as most consumer related commitments can be cancelled by the Group and non-consumer related commitments are entered into subject to the customer continuing to achieve specific credit standards. The Group is also exposed to credit risk from its derivatives, available for sale financial assets and other financial assets.

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 the CRPC and, where necessary, approved by the BRC or the Board. 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.

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 2017 of £2.8 billion include £1.4 billion due from the Parent, while deposits from banks at 31 December 2017 of £3.6 billion include £2.0 billion due to the Parent. At 31 December 2017, the Group therefore has a net exposure due to the Parent of £595 million (31 December 2016: £126 million net exposure due from the Parent).

At 31 December 2017, derivative assets and derivative liabilities include £20 million and £63 million respectively with the Parent and therefore a net exposure due to the Parent of £43 million (31 December 2016: £39 million net exposure due to the Parent).

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:

2.1.1 Definition of credit risk (continued)

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 in 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.

2.1.2 Credit risk management

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) has responsibility for credit management of the retail lending book, business banking book and the Northridge book. Supported by Directors / Heads of Retail Credit and Commercial Credit and the broader risk function, the CCO is responsible for overall credit risk reporting to the ERC, the BRC and the Board. The CCO reports to the CRO, who reports directly to the CEO. The broader 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.

Credit policy
The core values and principles governing the provision of credit are contained in the Credit Policy and Credit Framework, which are approved by the 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 in the policy documents.

Lending authorisation *(audited)*
The Group's credit risk management systems operate through a hierarchy of lending authorities, which are related to internal customer loan ratings and limits. In some consumer lending this includes the use of credit decisioning models, which are subject to strict governance processes. All exposures which exceed prescribed levels require approval or ratification by the 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.
All credit transactions are assessed at origination for credit quality and the borrower is assigned a credit grade based on a predefined credit rating scale. The risk, and consequently the credit grade, is reassessed periodically. The use of internal credit rating models and scoring tools, which measure the relative degree of risk inherent in lending to specific counterparties, is central to the credit risk assessment and ongoing management processes in the Group. Details of these internal credit rating models are outlined in the section on Credit risk methodologies on pages 51 to 55.

Counterparty credit risk
The continued weak international financial environment means that the Group continues to be exposed to increased counterparty risk. The Group has a number of measures in place 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 tight 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 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. In addition, derivatives executed with the Parent are subject to International Swaps and Derivatives Association (ISDA) and Credit Support Annex (CSA) standard documentation 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.

The 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 ongoing credit review and exposures are reported and monitored on a daily basis.

Loan loss provisioning
Through its ongoing 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

2.1.2 Credit risk management (continued)

and consistently across the loan book. For those loans that become impaired, the focus is on implementing appropriate work-out strategies, including consideration of vulnerable customers (see Section 2.8 on page 63), which minimise the loss that the Group will incur from such impairment. This may involve entering into restructuring arrangements with borrowers, or taking action to enforce security.

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 the BRC. Subsidiary impairment policies for individual business units are approved by the CRPC.

The Group's provisioning methodology is reviewed by the CRPC on a half yearly basis, details of which are set out in the Credit risk methodologies section on pages 51 to 55. The quantum of the Group's impairment charge, impaired loan balances, and provisions are also reviewed by the BRC on a half-yearly basis, in advance of providing a recommendation to the Audit Committee.

An analysis of the Group's impairment provisions at 31 December 2017 is set out on pages 41 to 44 and note 17.

2.1.3 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. In the commercial portfolio, regular risk reassessments are conducted on larger cases in line with policy.

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 collateral 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 (PD).

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.

A variety of types of collateral are accepted, as follows:
- residential and commercial real estate;
- physical assets (motor vehicles, plant and machinery, stock etc.);
- financial assets (lien over deposits, shares etc.); and
- other assets (debentures, 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 45. Details of the valuation methodologies are set out in the Credit provisioning methodologies section on page 52.

2.1.4 Credit risk reporting and 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, 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 the 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 and the BRC as required. GCR, an independent function within GIA, reviews the quality and management of credit risk assets across the Group and reports to the CRPC on a half yearly basis.

Regular portfolio review meetings covering the NI and GB commercial challenged portfolios are also conducted.

Group risk personnel as well as business 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 BRC, the Parent's Credit Risk function and the Parent's Group Risk Policy Committee (GRPC). Impairment provisioning methodologies are approved on a half yearly basis by the 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 or negative market price movements.

2.1.5 Management of challenged assets

A range of initiatives, dependent on the nature of the risk, are in place to deal with the effects of the deterioration in the credit environment and decline in asset quality including:

- collections and recoveries processes;
- utilisation of specialist work-out teams to ensure early intervention in vulnerable cases;
- intensive review cycles for 'at risk' exposures and the management of excess positions;
- support from central teams in managing 'at risk' portfolios at a business unit level;
- modified and tighter lending criteria for specific sectors;
- a reduction in certain individual bank exposures; and
- revised Risk Appetite Framework and Statement.

The segregation of certain challenged portfolios and the realignment of resources to manage these assets allows the remaining portfolio managers to focus on the loan book classified as 'acceptable quality' or better and to work closely with those customers.

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. An exposure continues to be classified as forborne until such time as it satisfies conditions to exit forbearance in line with EBA guidance.

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 to 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 being 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 loan 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 in the appropriate 'past due but not impaired' or 'neither past due nor impaired' rating category as described on page 42.

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.

The forbearance strategies adopted by the Group seek to maximise recoveries and minimise losses arising from non repayment of debt, while providing suitable and sustainable restructure options that are supportive of customers in challenged circumstances. The Group has an operating infrastructure in place to assess and, where appropriate, implement such options on a case-by-case basis. Group credit policy outlines the core principles and parameters underpinning the Group's approach to forbearance with individual business unit policies defining in greater detail the forbearance strategies appropriate to each unit.

Forbearance requests are assessed on a case-by-case basis taking due consideration of the individual circumstances and risk profile of the customer to ensure, where possible, the most suitable and sustainable repayment arrangement is put in place (see also section 2.8 on page 63 which further comments on vulnerable customers). Forbearance will always be a trigger event for the Group to undertake an assessment of the customer's financial circumstances and ability to repay prior to any decision to grant a forbearance treatment. This assessment may result in a disimprovement in the credit grade assigned to the loan, potentially impacting how frequently the loan must be formally

2.1.5 Management of challenged assets (continued)

reviewed; and, where impairment is deemed to have occurred, will result in a specific provision. Where appropriate, and in accordance with the Group's credit risk management structure, forbearance requests are referred to credit units for independent assessment prior to approval by the relevant approval authority.

Forborne loans are reviewed in line with the Group's credit management processes, which include monitoring borrower compliance with the revised terms and conditions of the forbearance arrangement. Loans to which forbearance has been applied continue to be classified as forborne until it meets the relevant exit criteria in line with EBA guidance.

Borrower compliance with revised terms and conditions may not be achieved in all cases. Non-compliance could for example arise because the individual circumstances and risk profile of the borrower continue to deteriorate, or fail to show an expected improvement, to the extent that an agreed reduced level of repayment can no longer be met. In the event of non-compliance, a request for further forbearance may be considered. It is possible that the Group, by virtue of having granted forbearance to a borrower, could suffer a loss that might otherwise have been avoided had enforcement action instead been taken. This could for example arise where the value of security held in respect of a loan diminishes over the period of a forbearance arrangement which ultimately proves unsustainable.

2.1.6 Book profile - loans and advances to customers

The Group's residential mortgage portfolio amounted to 80% of total loans at 31 December 2017 (31 December 2016: 79%). By product type, the residential mortgage portfolio is made up of standard owner occupier (61%), self-certified owner occupier (5%) and Buy to Let (BTL) (34%) (31 December 2016: 61%, 6%, and 33% respectively). In terms of geographical concentrations, the largest concentration is the London and South East area at 44% (31 December 2016: 47%) with the remainder as follows: South West 9%; North West 9%; East Midlands 6%; West Midlands 6%; Scotland 5%; Yorkshire & Humberside 6%; Northern Ireland 5%; East Anglia 4%; North 3%; and Wales 3%. Product type and geographic concentrations are monitored and reported in accordance with the monetary limits set by the BRC.

The property and construction sector, which includes investment property and landbank, accounted for 3%, or £0.7 billion of total loans at 31 December 2017 (31 December 2016: 5% or £1 billion).

Total loans - by industry analysis *(audited)*	**2017 £m**	2016 £m
Residential mortgages	16,043	15,964
Finance leases and hire purchase	1,411	1,227
Credit cards	625	663
Personal loans	327	87
Commercial property and construction	652	961
Business and other services	731	865
Manufacturing and distribution	356	292
Other	7	28
Total	**20,152**	20,087

The following table provides a spilt of the Group's impairment provision at 31 December 2017 and 31 December 2016 between specific and incurred but not reported (IBNR).

Specific provisions decreased by 49% to £108 million at 31 December 2017, (31 December 2016: £211 million) mainly as a result of provision utilisation in the commercial portfolio. IBNR provisions decreased from £55 million at 31 December 2016 to £47 million at 31 December 2017. This year on year decrease of 15% primarily relates to deleveraging in the commercial banking portfolio.

Impairment provision by nature of impairment provision *(audited)*	**2017 £m**	2016 £m
Specific provisions	108	211
Incurred but not reported (IBNR)	47	55
Total impairment provision	**155**	266

2.1.6 Book profile - loans and advances to customers (continued)

In the following table the impairment charges for the years to 31 December 2017 and 31 December 2016 are analysed by asset classification.

During 2017, actual loan losses continued to fall and conditions improved in some property sectors / regions.

Impairment charges on loans and advances to customers increased by £3 million from £23 million for the year ended 31 December 2016 to £26 million for the year ended 31 December 2017.

The impairment charge on residential mortgages of £2 million remained flat year on year.

The impairment charge on the non-property SME and corporate loan portfolio was c.£1 million for the year ended 31 December 2017 (31 December 2016: £nil).

The impairment charge of £8 million on the commercial property and construction portfolio, for the year ended 31 December 2017, has decreased from £17 million for the year ended 31 December 2016 as a result of a continued improvement in the commercial and residential property sectors and successful recovery activities as well as the benefit of IBNR release.

The impairment charge of £15 million on consumer loans for the year ended 31 December 2017 has increased in line with forecasted growth and maturity of the portfolio by £11 million from £4 million for the year ended 31 December 2016.

Impairment charge *(audited)*	2017 Specific £m	2017 IBNR £m	2017 Total £m	2016 Specific £m	2016 IBNR £m	2016 Total £m
Residential mortgages	1	1	2	3	(1)	2
Non-property SME and corporate	4	(3)	1	7	(7)	-
Commercial property and construction	15	(7)	8	20	(3)	17
Consumer (excluding mortgages)	12	3	15	5	(1)	4
Total loan impairment charge / (release)	**32**	**(6)**	**26**	**35**	**(12)**	**23**

2.1.7 Asset quality - loans and advances to customers

Asset quality - loans and advances to customers
The Group has revised its asset quality reporting methodology to align with EBA guidance on non-performing and forborne classifications[1].

Previously the Group did not apply a set time period after which the forborne classification on a performing loan was discontinued. Exit criteria are now applied In line with EBA guidance.

All exposures that are subject to forbearance and have a specific provision are reported as both forborne and impaired whereas previously in the non-mortgage portfolios where an exposure carried a specific provision it was reported as 'impaired' and not reported as 'forborne'.

The Group's definition of impaired loans has been modified to remove non-mortgage loans that are greater than 90 days in arrears but where a specific provision is not required, instead these loans are now classified as 'greater than 90 days in arrears and not impaired'

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 thirteen point credit rating scale based on PD is used for residential mortgages. A seven-point credit grade rating scale is used for standard products (including personal and small business loans). Both credit scales have a defined relationship with the Group's 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 applied 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 SMEs, 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

[1] *In particular the EBA's 'Implementing Technical Standards on supervisory reporting on forbearance and non-performing exposures.*

2.1.7 Asset quality - loans and advances to customers (continued)

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 in 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.

'Impaired' loans are defined as exposures which carry a specific provision whether forborne or not. Specific provisions are as a result of either individual or collective assessment for impairment.

Past due but not impaired:
Past due but not impaired loans, whether forborne or not, are defined as follows:

- Loans where repayment of interest and / or principal are overdue by at least one day but which are not impaired.

Refer to page 51 for details on the loan loss provisioning methodology.

The following tables provide an asset quality analysis of loans and advances to customers before impairment provisions by asset classification as at 31 December 2017 and 31 December 2016.

2017 Risk profile of loans and advances to customers (before impairment provisions) *(audited)*	**Residential mortgages £m**	**Non-property SME and corporate £m**	**Commercial property and construction £m**	**Consumer £m**	**Total loans and advances customers £m**	**Total loans and advances customers %**
High quality	15,583	478	116	2,039	18,216	90%
Satisfactory quality	23	588	180	-	791	4%
Acceptable quality	38	169	95	-	302	2%
Lower quality but not past due nor impaired	-	48	88	-	136	1%
Neither past due nor impaired	**15,644**	**1,283**	**479**	**2,039**	**19,445**	**97%**
Past due but not impaired	332	38	39	23	432	2%
Impaired	67	50	134	24	275	1%
Total	**16,043**	**1,371**	**652**	**2,086**	**20,152**	**100%**

2016 Risk profile of loans and advances to customers (before impairment provisions) *(audited)*	Residential mortgages[1] £m	Non-property SME and corporate £m	Commercial property and construction £m	Consumer £m	Total loans and advances customers £m	Total loans and advances customers %
High quality	15,483	572	110	1,671	17,836	89%
Satisfactory quality	20	583	221	-	824	4%
Acceptable quality	42	99	137	-	278	2%
Lower quality but not past due nor impaired	-	84	175	-	259	1%
Neither past due nor impaired	15,545	1,338	643	1,671	19,197	96%
Past due but not impaired[2]	352	35	51	19	457	2%
Impaired[2]	67	80	267	19	433	2%
Total	15,964	1,453	961	1,709	20,087	100%

[1] *As described on pages 42 and 43, the Group has revised its asset quality reporting methodology to align with EBA guidance on non-performing and forborne classifications. As a result, the Group has amended the risk profile of Residential mortgages which are neither 'past due nor impaired' to reflect this change in classification and comparative figures have been restated resulting in an increase in the 'high quality' by £48 million from £15,435 million with offsetting decreases in 'satisfactory quality' by £5 million from £25 million, 'acceptable quality' by £31 million from £73 million and 'lower quality' by £12 million from £12 million, with no change to the overall total of 'neither past due nor impaired' loans.*

[2] *As described on pages 42 and 43, the Group has modified its definition of impaired loans with a corresponding impact on amounts classified as 'past due greater than 90 days but not impaired'. As a result comparative figures have been restated as follows; impaired 'Non-property SME and corporate' have reduced by £20 million (from £100 million to £80 million) with a corresponding increase in amounts classified as 'past due but not impaired' (from £15 million to £35 million) and impaired 'Commercial property and construction' loans have reduced by £22 million (from £289 million to £267 million) with a corresponding increase in amounts classified as 'past due but not impaired' (from £29 million to £51 million)*

2.1.7 Asset quality - loans and advances to customers (continued)

Financial assets - 'past due but not impaired': loans and advances to customers

The tables below provide an aged analysis of financial assets 'past due but not impaired', by asset classification as at 31 December 2017 and 31 December 2016. Amounts arising from operational / timing issues, that are outside the control of customers, are generally excluded.

2017 **Financial assets - 'past due but not impaired': loans and advances to customers** *(audited)*	**Residential mortgages £m**	**Non-property SME and corporate £m**	**Commercial property and construction £m**	**Consumer £m**	**Total £m**
Past due up to 30 days	107	6	1	13	127
Past due 31-60 days	145	7	21	8	181
Past due 61-90 days	29	2	2	2	35
Past due more than 90 days but not impaired	51	23	15	-	89
Total	**332**	**38**	**39**	**23**	**432**

2016 Financial assets - 'past due but not impaired': loans and advances to customers (audited)	Residential mortgages £m	Non-property SME and corporate £m	Commercial property and construction £m	Consumer £m	Total £m
Past due up to 30 days	97	5	3	10	115
Past due 31-60 days	159	5	17	7	188
Past due 61-90 days	37	5	9	2	53
Past due more than 90 days but not impaired[1]	59	20	22	-	101
Total	352	35	51	19	457

There was a decrease in the total 'past due, but not impaired' balances from £457 million to £432 million primarily due to improved positions in the commercial property and construction and residential mortgages portfolios. Arrears on residential mortgages decreased by £20 million, predominantly in the self-certified segment.

2017 **Financial assets - 'impaired': loans and advances to customers** *(audited)*	**Advances £m**	**Impaired loans £m**	**Impaired loans as a % of advances %**	**Specific provisions £m**	**Specific provisions as % of impaired loans %**
Residential mortgages	16,043	67	-	7	10%
Non-property SME and corporate	1,371	50	4%	26	52%
Commercial property and construction	652	134	21%	59	44%
Consumer (excluding mortgages)	2,086	24	1%	16	67%
Total	**20,152**	**275**	**1%**	**108**	**39%**

2016 Financial assets - 'impaired': loans and advances to customers *(audited)*	Advances £m	Impaired loans[1] £m	Impaired loans as a % of advances %	Specific provisions £m	Specific provisions as % of impaired loans %
Residential mortgages	15,964	67	-	8	12%
Non-property SME and corporate	1,453	80	6%	49	61%
Commercial property and construction	961	267	28%	140	52%
Consumer (excluding mortgages)	1,709	19	1%	14	74%
Total	20,087	433	2%	211	49%

[1] *Comparative figures have been restated as set out on pages 42 and 43.*

2.1.7 Asset quality - loans and advances to customers (continued)

Loans and advances to customers classified as 'impaired' amounted to £275 million, representing 1% of the Group's total loan book at 31 December 2017 (31 December 2016: £433 million and 2%).

Commercial property and construction loans classified as 'impaired' reduced by £133 million during the year, primarily as a result of the impacts of provision utilisation through completion of work-out strategies. However, impaired loans in the commercial property and construction portfolio remain elevated at £134 million at 31 December 2017 (31 December 2016: £267 million), reflecting continued weak conditions in some segments of the investment property loan portfolio as well as the difficulties facing the residential land sector, particularly in Northern Ireland.

The volume of non-property SME and corporate loans that are classified as 'impaired' reduced, from £80 million at 31 December 2016, to £50 million at 31 December 2017. This decrease reflects cases closed out through conclusion of work-out strategies resulting in either successful recovery, refinance, or provision utilisation following realisation of underlying security.

Consumer loans classified as 'impaired' have increased from £19 million to £24 million at 31 December 2017. This reflects the forecasted growth and maturity of the personal loan portfolio since inception in 2015.

The following tables set out an analysis of the LTV profile of the Group's residential mortgage portfolio as at 31 December 2017 and 31 December 2016.

2017 **Loan to value (LTV) ratio of total mortgages** *(audited)*	**Standard % of book**	**Buy to let % of book**	**Self certified % of book**	**Total mortgage portfolio % of book**
Less than 50%	23%	33%	38%	27%
51% to 70%	35%	48%	38%	40%
71% to 80%	18%	14%	13%	17%
81% to 90%	19%	4%	7%	13%
91% to 100%	5%	1%	4%	3%
Subtotal	**100%**	**100%**	**100%**	**100%**
101% to 120%	-	-	-	-
Greater than 120%	-	-	-	-
Total	**100%**	**100%**	**100%**	**100%**
Weighted average LTV[1]:				
Stock of mortgages at year end	64%	56%	56%	61%
New mortgages during year	74%	60%	-	72%

2016 Loan to value (LTV) ratio of total mortgages *(audited)*	Standard % of book	Buy to let % of book	Self certified % of book	Total mortgage portfolio % of book
Less than 50%	23%	33%	35%	27%
51% to 70%	37%	44%	37%	40%
71% to 80%	21%	15%	13%	18%
81% to 90%	14%	5%	9%	11%
91% to 100%	4%	2%	5%	3%
Subtotal	**99%**	**99%**	**99%**	**99%**
101% to 120%	-	-	-	-
Greater than 120%	1%	1%	1%	1%
Total	100%	100%	100%	100%
Weighted average LTV[1]:				
Stock of mortgages at year end	63%	57%	58%	61%
New mortgages during year	73%	62%	-	71%

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

2.1.7 Asset quality - loans and advances to customers (continued)

Forbearance arrangements for residential mortgages *(audited)*
The tables below illustrate residential mortgages that have been subject to restructuring arrangements during 2017 and 2016.

2017	**Performing[1]**		**Non-performing exposures**		**All loans**	
Forbearance arrangements - residential mortgages (before impairment provisions) (audited)	**Balance £m**	**Number of accounts[3]**	**Balance £m**	**Number of accounts[3]**	**Balance £m**	**Number of accounts[3]**
Term extension	16	158	2	24	18	182
Interest only	7	48	41	358	48	406
Capitalisation of arrears	9	54	2	11	11	65
Other	6	49	8	68	14	117
Total	**38**	**309**	**53**	**461**	**91**	**770**

2016	Performing[1]		Non-performing exposures		All loans	
Forbearance arrangements - residential mortgages (before impairment provisions)[2] (audited)	Balance £m	Number of accounts[3]	Balance £m	Number of accounts[3]	Balance £m	Number of accounts[3]
Term extension	12	126	2	35	14	161
Interest only	8	71	44	388	52	459
Capitalisation of arrears	9	55	2	13	11	68
Other	6	57	10	75	16	132
Total	35	309	58	511	93	820

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 pages 40 to 41.

[1] *Loans neither > 90 days past due nor impaired*
[2] *In line with the revised asset reporting methodology as set out on pages 42 and 43, the comparative figures for forborne residential mortgages have been restated, resulting in an increase in total forborne residential mortgages from £727 million to £820 million*
[3] *The number of accounts does not equate to either the number of customers or the number of properties.*

2.1.7 Asset quality - loans and advances to customers (continued)

Forbearance arrangements for commercial loans *(audited)*
The following tables illustrate commercial loans that have been subject to restructuring arrangements during 2017 and 2016. 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.

2017	**Commercial property and construction**				**Total**
Forbearance arrangements (before impairment provisions) (audited)	**Land and development £m**	**Investment £m**	**Total £m**	**Non-property SME and corporate £m**	**forborne loans and advances customers £m**
Term extension	31	163	194	76	270
Adjustment or non-enforcement of covenants	-	-	-	3	3
Interest only	1	8	9	4	13
Facilities in breach of terms placed on demand	-	3	3	-	3
Reduced payment (greater than interest only)	-	1	1	-	1
Other	8	13	21	18	39
Total forborne loans and advances to customers	**40**	**188**	**228**	**101**	**329**

2016	Commercial property and construction				Total
Forbearance arrangements (before impairment provisions)[1] (audited)	Land and development £m	Investment £m	Total £m	Non-property SME and corporate £m	forborne loans and advances customers £m
Term extension	24	211	235	75	310
Adjustment or non-enforcement of covenants	-	1	1	7	8
Interest only	3	21	24	5	29
Facilities in breach of terms placed on demand	2	69	71	17	88
Reduced payment (greater than interest only)	-	26	26	4	30
Other	69	65	134	47	181
Total forborne loans and advances to customers	98	393	491	155	646

Commercial property and construction

(a) *Investment*

This category represents 57% of the total forborne commercial loans at 31 December 2017, which reflects the impact of the sizeable downward adjustment in property prices since the loans were approved and drawn. The need for forbearance was principally caused by a fall in property values rather than reduced rental income. 'Term extensions' account for 87% of all forbearance measures granted in this category, which reflects our experience that granting customers additional time is often the most likely means by which repayment may be achieved, either through ongoing receipt of rents or via eventual property disposal. Property loan repayments are not normally reduced unless the rental income generated by the property decreases; consequently, 'reduced payments' (including interest-only arrangements) only account for 5% of forbearance measures in this category.

(b) *Land & Development (L&D)*

The L&D book has significantly reduced during the year and now accounts for only 12% of total forborne loans. 'Term extension' was the most common type of forbearance granted (78% of the total).

Non-property, SME and Corporate

This category accounts for 31% of total forborne loans. Forbearance measures have been granted to 11% of SME and corporate exposures, compared to 32% for investment property and 57% for L&D. This is consistent with the generally stronger credit quality of SME and corporate sector exposures compared to those in the commercial property and construction sector. It also partly reflects the greater number of options typically available to the SME and 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 'term extensions' (75%) and 'other' measures (18%); such as weakening of the security structure.

[1] *In line with the revised asset reporting methodology as set out on pages 42 and 43, the comparative figures for forborne commercial loans have been restated, resulting in an increase in total forborne commercial loans from £471 million to £646 million.*

2.1.7 Asset quality - loans and advances to customers (continued)

Repossessed collateral on residential mortgages
At 31 December 2017 and 31 December 2016 the Group held collateral as security on residential mortgages as detailed in the table below.

	2017		2016	
Repossessed collateral - residential mortgages *(audited)*	**Number of repossessions as at balance sheet date**	**Balance outstanding £m**	Number of repossessions as at balance sheet date	Balance outstanding £m
Residential repossessions				
Owner occupier	13	2	17	2
Buy to let	17	2	11	1
Self certified	6	2	4	1
Total	**36**	**6**	**32**	**4**

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

During the year ended 31 December 2017 the Group disposed of 57 repossessed properties. The total contracted disposal proceeds were adequate to cover the balance outstanding after provisions.

2017 Repossessed collateral - residential mortgages *(unaudited)*	**Number of disposals during the year**	**Balance outstanding at repossession £m**	**Net sales proceeds received £m**
Residential repossessions			
Owner occupier	28	2	3
Buy to let	25	2	3
Self certified	4	1	1
Total	**57**	**5**	**7**

Repossessed collateral on property and construction loans

	2017		2016	
Repossessed collateral - property and construction *(audited)*	**Number of repossessions as at balance sheet data**	**Balance outstanding £m**	Number of repossessions as at balance sheet data	Balance outstanding £m
Property and construction	2	-[1]	3	1
Total	**2**	**-**	**3**	**1**

Repossessed properties are sold as soon as practicable, with the proceeds applied against outstanding indebtedness.
During the year ended 31 December 2017 the Group disposed of one repossessed property[2]. The total contracted disposal proceeds were adequate to cover the balance outstanding after provisions.

2017 **Repossessed collateral - property and construction** *(unaudited)*	**Number of disposals during the year**	**Balance outstanding at repossession £m**	**Net sales proceeds received £m**
Property and construction	1	1	1
Total repossessions	**1**	**1**	**1**

[1] *The balance outstanding on repossessed collatered is c.£120k*
[2] *The number of properties disposed of during the year ended 31 December 2017 includes those which were subject to an unconditional contract for sale at year end date.*

2.1.8 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 by external agencies, or are assigned an internal rating based on the Parent's internal models, or a combination of both. Mappings to Moody's external ratings in the table below, are therefore indicative only.

Asset quality: Other financial instruments with ratings equivalent to *(audited)*	**2017 £m**	2016 £m
Aaa to Aa3	2,358	2,328
A1 to A3	23	149
Baa1 to Baa3	1,418	2,087
Total	**3,799**	**4,564**

Exposures by country

The following tables provide 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 2017 and 31 December 2016. In addition, for these line items, further information is included on the Group's exposures to selected countries and their associated credit ratings from Moody's.

Asset quality: exposures by country 2017 *(audited)*	**Credit rating[1]**	**Cash and balances[2] £m**	**Loans and advances to banks[3] £m**	**Available for sale financial assets[4] £m**	**Derivative financial instruments £m**	**Total £m**
Ireland	A2	-	1,394	-	20	1,414
United Kingdom	Aa2	1,836	1,237	602	7	3,682
Other		-	133	406	-	539
Total		**1,836**	**2,764**	**1,008**	**27**	**5,635**

Asset quality: exposures by country 2016 *(audited)*	Credit rating[1]	Cash and balances[2] £m	Loans and advances to banks[3] £m	Available for sale financial assets[4] £m	Derivative financial instruments £m	Total £m
Ireland	A3	-	2,038	-	50	2,088
United Kingdom	Aa1	1,172	1,191	726	5	3,094
Finland	Aa1	-	-	45	-	45
Other		-	140	369	-	509
Total		1,172	3,369	1,140	55	5,736

[1] *Based on credit ratings from Moody's.*
[2] *Cash and balances in the United Kingdom primarily consist of amounts placed with the Bank of England.*
[3] *Loans and advances to banks in Ireland consist primarily of balances with the Parent and balances in the United Kingdom consist primarily of the Bank of England required collateral for notes in circulation. Loans and advances to banks in Ireland reduced by 32% during the year from £2 billion at 31 December 2016 to £1.4 billion at 31 December 2017. 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.*
[4] *Available for sale financial assets consist of UK Government gilts, Finnish government paper, Supranational bonds and UK covered bonds.*

2.1.8 Asset quality - other financial instruments (continued)

The following tables provide a maturity analysis of the Group's exposures to Ireland and the United Kingdom at 31 December 2017 and 31 December 2016.

2017 **Other financial instruments** **Ireland** *(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	434	275	389	279	17	-	1,394
Total	**434**	**275**	**389**	**279**	**17**	**-**	**1,394**

2016 Other financial instruments Ireland	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	495	448	410	668	17	-	2,038
Total	495	448	410	668	17	-	2,038

2017 **Other financial instruments** **United Kingdom** *(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 with central banks	1,836	-	-	-	-	-	1,836
Loans and advances to banks	1,237	-	-	-	-	-	1,237
Available for sale financial assets	20	51	229	302	-	-	602
Total	**3,093**	**51**	**229**	**302**	**-**	**-**	**3,675**

2016 Other financial instruments United Kingdom	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 with central banks	1,172	-	-	-	-	-	1,172
Loans and advances to banks	1,191	-	-	-	-	-	1,191
Available for sale financial assets	-	123	72	478	53	-	726
Total	2,363	123	72	478	53	-	3,089

As set out in the Group's accounting policies on pages 84 to 98, 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 reserve in stockholder's equity; and
- loans and advances to banks and cash and balances with central banks are held at amortised cost.

2.1.9 Credit risk methodologies (audited)

Loan loss provisioning methodology
Through its ongoing 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 'workout' strategies.

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.

Commercial 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 in the Bank and 60 days in arrears in Northridge or which meet the other EBA guidelines on non-performing and forborne classification are included in non-performing exposures.

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.

International Accounting Standards (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 (DCF) 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 forecast 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.

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 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 IBNR 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 PD);
- the emergence period (historic experience adjusted to reflect the current conditions and the credit management model); and
- Loss Given Default (LGD) 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

2.1.9 Credit risk methodologies (audited) (continued)

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.

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 2017 is set out on pages 40 to 41 and pages 46 to 47. 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 on a six monthly basis, 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 2017 is set out on pages 41 to 44 and note 17.

Credit management process
For consumer and lower value commercial exposures, the review is largely based on account behaviour and is highly automated. Where there are loan arrears, excesses, dormancy 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 reaffirms 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 used in the IBNR calculation is calculated using historical loan loss experience. The range of emergence periods is typically three to twelve months (consumer lending products twelve months; commercial property and commercial / SME lending three to four months).

The LGD used in the IBNR calculation 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 ongoing 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 the BRC.

The Group's provisioning methodology is reviewed by the CRPC on a half yearly basis. The quantum of the Group's impairment charge, impaired loan balances, and provisions are also reviewed by the BRC on a half-yearly basis, 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 and use of automated valuations - residential mortgages
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 61% at 31 December 2017 (31 December 2016: 61%). 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. In line with others in the industry, the Group uses automated house price valuations to assess collateral positions in monitoring

2.1.9 Credit risk methodologies (audited) (continued)

certain cohorts of the book.

(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*
Valuation policy permits the use of internally assessed valuations where appropriate. 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. Assessed values are subject to oversight by the independent credit unit.

(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.

IFRS 9 ‘Financial Instruments’
(unaudited)
IFRS 9: ‘Financial instruments’ is effective for annual periods commencing on or after 1 January 2018. The Bank of Ireland Group’s IFRS 9 Programme has been in existence since 2015 and extensive information on the progress of IFRS 9 implementation has been given in the Group’s Annual Report and the Parent’s Annual and Interim Reports since then.

Overall implementation
Development work on the IFRS 9 technology infrastructure, operating model and governance, and the expected credit losses (ECL) or impairment model suite is largely completed. Successful completion of system integration testing and user acceptance testing of each component of the end-to-end technical solution in the last quarter of 2017 supported the Group’s readiness for compliance with IFRS 9 from 1 January 2018. Further refinement of the technology infrastructure will continue during 2018.

Classification and measurement
The Group has completed its assessment of business models and the contractual cash flow characteristics of financial assets. There was no change in measurement basis for the majority of the Group’s financial assets. However, the liquid asset bonds currently classified as available for sale financial assets will be reclassified to amortised cost under IFRS 9 as they are part of a hold to collect business model.

IFRS 9 business models have been defined based on:
- how groups of financial assets are managed together;
- how their performance is evaluated and reported to key management personnel;
- how risks are managed; and
- intentions about future sales.

Sales of financial assets close to maturity or due to an increase in credit risk, or infrequent sales of significant volumes of financial assets, are consistent with a hold-to collect business model. Based on recent experience, the volume of sales of financial assets from the Group’s hold-to-collect business models has been insignificant.

Under IFRS 9, the changes in the fair value of liabilities designated at fair value through profit or loss arising from changes in own credit spread are no longer recognised in the income statement but are instead recognised in other comprehensive income, unless this would create or enlarge an accounting mismatch in profit or loss.

Hedge accounting
The Group has made the accounting policy choice allowed under IFRS 9 to continue to apply the hedge accounting requirements of IAS 39 until the amended standard resulting from an IASB project on macro hedge accounting becomes effective. However, new hedge accounting disclosures will still be required by related amendments to IFRS 7 ‘Financial Instruments: Disclosure’.

Impairment
The Impairment Policy applicable under IFRS 9 was approved by the Board Risk Committee in November 2017 to support business readiness by its effective date of 1 January 2018. It outlines the Group’s over-arching policies in respect of the impairment of financial instruments under IFRS 9 and is applicable to all business units within the Group.

Impairment models and forward looking information
Development of the Group’s suite of IFRS 9 impairment models has concluded, and independent validation and testing is also complete. In the second half of 2017, the impairment models were approved for use by the IFRS 9 Programme Governance, enabling the impairment models to be used in the measurement of the initial IFRS 9 impairment loss allowance and stage allocation at 1 January 2018.

Forward looking information (FLI) refers to probability-weighted future macroeconomic scenarios used in the

2.1.9 Credit risk methodologies (audited) (continued)

assessment of significant increase in credit risk and in the measurement of impairment loss allowances under IFRS 9. Three FLI scenarios (a central, an upside and a downside scenario) and associated probability weightings have been approved by the Executive Risk Committee (ERC). These scenarios have been incorporated into the impairment models to calculate the initial IFRS 9 impairment loss allowance and stage allocation at 1 January 2018. The scenarios include forecasts of variables such as GDP, unemployment and property prices.

FLI scenarios and associated probability weightings will be updated and approved semi-annually by the ERC. On an annual basis the Board will review and approve the central FLI scenario as part of its strategic planning.

Staging
The Group's standard staging criteria under IFRS 9 apply to the vast bulk of loans and advances to customers. A financial asset which is not credit-impaired and has not experienced a significant increase in credit risk since initial recognition is allocated to stage 1 and is subject to an impairment loss allowance equal to 12-months ECL. The Group's standard criteria to determine if there has been a significant increase in credit risk since initial recognition, leading to stage 2 (unless credit-impaired which is stage 3) and an impairment loss allowance equal to lifetime ECL, incorporate quantitative and qualitative factors. These factors include:

- more than a doubling of remaining life time PD (subject to an absolute minimum movement);
- whether a financial instrument is forborne or is a non-performing exposure; and
- whether a financial instrument is greater than 30 days past due.

The standard staging criteria are automatically applied as part of the monthly execution of the Group's impairment models, with each financial instrument allocated to a stage. The Group intends to assess the effectiveness of its staging criteria semi-annually and to revise the criteria if appropriate.

The Group applies the low credit risk expedient to most debt securities in scope for the impairment requirements of IFRS 9 and similarly to loans and advances to banks, central banks and investment firms. 'Low credit risk' encompasses PD grades 1 to 5 on the Group's internal PD rating system, which broadly aligns with ratings of AAA to BBB- for the external major rating agencies. Such financial instruments are allocated to stage 1.

From 1 January 2018, the manner in which the Group identifies financial assets as credit-impaired (stage 3, with an impairment loss allowance equal to lifetime ECL) under IFRS 9 results in the Group's population of credit-impaired financial assets being consistent with its population of financial assets in regulatory default. Therefore all financial assets in regulatory default within the scope of the impairment requirements of IFRS 9 are classified as credit-impaired.

In summary, an exposure is considered to be in default if: (a) the borrower is considered unlikely to pay in full without recourse by the Group to actions such as realising security (including 'forborne collateral realisation' loans and loans which would have been considered impaired under IAS 39); and / or (b) the borrower is greater than 90 days past due and the arrears amount is material.

The population of credit-impaired financial assets that will be reported under IFRS 9 will be broader than the population of impaired loans reported under the definition used by the Group under IAS 39, which equates to loans with a specific provision. The population of non-performing exposures will be broader than the population of credit-impaired financial assets reported under IFRS 9, as it will include other loans meeting non-performing exposure criteria, in line with EBA guidance, such as probationary loans that have yet to satisfy exit criteria to return to a performing classification. The quantum of non-performing exposures is unchanged on transition to IFRS 9.

Operating model and governance
Work has concluded on the IFRS 9 operating model and governance framework, leveraging existing arrangements where appropriate and ensuring consistency with the Group's three lines of defence approach to risk management. The impairment operating model is more centralised, and where appropriate aligned with the Group's Parent. This is driven, in part, by some of the key requirements of IFRS 9 such as generating FLI and stage allocation. All governance committees' roles and responsibilities have been reviewed and updated in respect of impairment oversight. New and revised impairment business processes, including process controls, have been designed and put into operation.

Training and education briefings have been delivered to relevant internal stakeholders, ensuring business readiness for IFRS 9. This included the roll-out of web-based training for the Impairment Policy applicable under IFRS 9.

Practical expedients and policy choices
The Group has applied certain 'practical expedients' as allowed under IFRS 9 including:

- use of the low credit risk practical expedient (as outlined above);
- approximation of the 'credit risk at initial recognition' for in-scope financial instruments originated prior to certain dates in 2017;
- limiting certain information sets on the basis of undue cost or effort; and
- use of loss rates for certain smaller and / or lower risk portfolios.

In determining the appropriateness of practical expedients, the Group has been mindful of the requirement that ECL under IFRS 9 should reflect an unbiased amount and make use of reasonable and supportable information available without undue cost or effort.

The Group has decided not to make the accounting policy choice allowed under IFRS 9 to always measure the impairment loss allowance on lease receivables at an amount equal to lifetime ECL.

Quantitative impact and regulatory treatment

Quantitative impact
The estimated quantitative impact on initial adoption of IFRS 9 is a reduction in stockholders' equity of approximately c.£40 million after tax, which predominantly relates to an increase in impairment loss allowance on loans and advances to customers.

The key drivers of the change in impairment loss allowance include but are not limited to:

- the concept of 'stage 2' under IFRS 9 whereby loans which have experienced a significant increase in credit risk since initial recognition are subject to an impairment loss allowance equal to lifetime ECL, which generally exceeds incurred but not reported (IBNR) provisions recognised

2.1.9 Credit risk methodologies (audited) (continued)

under IAS 39;
- the incorporation of FLI in impairment calculations at 1 January 2018; and
- the requirement to recognise impairment on loan commitments from 1 January 2018.

The most adversely impacted portfolios are the Non-property SME and Corporate and Consumer portfolios reflecting impairment loss allowances equal to lifetime ECL on stage 2 assets (which generally exceed IBNR provisions recognised under IAS 39) and relatively large undrawn commitments within these portfolios.

The Group intends to provide the required detailed disclosures on the actual quantitative impact on the initial adoption of IFRS 9 (which may include refinement to the above estimate) by measurement category and financial asset class in the Annual Report for the year ended 31 December 2018. In accordance with the accounting policy choice allowed under IFRS 7 as amended by IFRS 9, comparative figures will not be restated.

Regulatory treatment
The Group has chosen to avail of the transitional arrangements for mitigating the impact of IFRS 9 on regulatory capital as outlined in the amended Capital Requirements Regulation. This allows the Group to add back to its regulatory Common Equity Tier 1 capital a proportion of the increase in impairment loss allowance on transition to IFRS 9 and also a proportion of any increase in stage 1 and 2 impairment loss allowance between transition and the relevant reporting date, subject to certain adjustments. The proportion to be added back is 95% in 2018 and 85%, 70%, 50% and 25% respectively in the subsequent 4 years with the relief ending on 31 December 2022. The Group has estimated that the quantitative impact from initial adoption of IFRS 9 on 1 January 2018 will reduce the Group’s fully loaded CET1 ratio by c.30 bps.

The transitional adjustment arising from the adoption of IFRS 9 is to be spread over 10 years for UK Corporation Tax.

2.2 Liquidity and funding risk

Key points:
- At all times during the financial year the Group maintained appropriate levels of unencumbered liquid resources and an appropriate liquidity position, in line with regulatory and internally set requirements and limits.
- The Group held liquid assets of £3 billion at 31 December 2017 which was in excess of regulatory liquidity requirements and within the Group’s internal risk appetite. This represented a prudent liquidity position.
- The Group's loan to deposit ratio increased from 102% at 31 December 2016 to 105% at 31 December 2017, which reflects the net effect of the efficient management of liquidity excess, drawdown from the Bank of England Term Funding Scheme and modest use of wholesale funding (including ILTR).
- The Group adhered to its policy of self-funding predominantly through retail deposits with no material funding dependency on the Parent or wholesale funding market.

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.

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 liquidity and funding risk appetite statement is set by the Board and is reviewed on an annual basis and sets out the level of liquidity and funding risk that the Board has deemed acceptable and the key liquidity and funding metrics that the Group has determined best define its liquidity and funding risk appetite.
The Group has established a liquidity and funding RMF, that is aligned to the Group’s risk appetite and risk targets, and which is aligned with its overall strategy to be a predominantly self-funded business, with no material funding dependency on the Parent or wholesale funding market.

The Group’s liquidity and funding RMF is designed to ensure that the Group manages and monitors its liquidity and

2.2 Liquidity and funding risk (continued)

funding position in accordance with the defined liquidity and funding risk appetite statement. The operational oversight and adherence to risk appetite is delegated to the ALCo, an executive subcommittee of the ERC.

The Group's ILAAP sets out how the Group assesses, quantifies and manages the key liquidity and funding risks 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, nature and duration.

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

- *Tactical liquidity management* - which focuses 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; 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
- *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.

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 signals.

Liquidity risk is measured using stress testing and scenario analysis. The Group runs a number of internal liquidity stress scenarios based on market-wide stress events, Group specific stress events and a combination of market-wide and idiosyncratic stress events. These stress scenarios are also performed across a number of outflow time bands. The daily cashflows resulting from the stress scenarios are compared against the holding of liquid assets. Under the Group's liquidity risk appetite, the Group must have unencumbered liquidity resources available which will be in excess of 100% of the stressed cashflows, from all stress scenarios performed.

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

Bank of England Term Funding Scheme (TFS)

The Group's funding structure also includes the utilisation of the Bank of England TFS. The TFS is designed to reinforce the transmission of bank rate cuts to the Group's lending and deposit interest rates and provide a cost effective source of funding to support additional lending to the real economy. This allows the Group to borrow central bank reserves in exchange for eligible collateral over a four year term.

The Group's funding from the TFS was £1.2 billion at 31 December 2017.

Customer deposits

The Group's funding strategy is focused, in particular, on maintaining a stable retail deposit base providing an appropriate basis to fund customer lending.

£13.9 billion of deposits at 31 December 2017 relates to Post Office branded deposits which decreased by £0.6 billion (4%) during the year. This is due to a combination of management actions to reduce the Group's overall liquidity excess and the utilisation of the Bank of England Term Funding Scheme and other wholesale funding.

The Group's loan to deposit ratio, as defined on page 7, increased from 102% at 31 December 2016 to 105% at 31 December 2017, as a result of the planned management actions.

Customer accounts *(unaudited)*	**2017 £m**	2016 £m
Bank of Ireland UK branded deposits	1,940	2,183
Bank of Ireland UK branded current accounts	2,800	2,513
Post Office branded deposits	13,924	14,567
AA branded deposits	297	212
Total	**18,961**	**19,475**

2.2 Liquidity and funding risk (continued)

Liquid assets
The Group maintains an unencumbered liquid asset portfolio, comprising cash placements and securities that can be used to raise liquidity, either by sale or through secured funding transactions.

As at 31 December 2017 the portfolio comprised cash balances with the Bank of England, UK Government Gilts, Supranational and Agency bonds, UK covered bonds and interbank placements.

The composition of the portfolio is set out below. Interbank placements comprised both placements with external banks and the Parent.

At 31 December 2017, £2.8 billion of the liquid asset portfolio is eligible to be applied in liquid asset stress testing (31 December 2016: £2.3 billion). The £2.8 billion eligible liquid assets do not include cash or general bank accounts that are utilised in the day to day operations of the Group.

In addition, the Group has a range of potential contingency funding actions that can be taken in the event of an unexpected shortfall in liquidity.

	Average in year		Year end	
Composition of the liquid asset portfolio *(unaudited)*	**2017 £m**	2016 £m	**2017 £m**	2016 £m
Balances with central banks	1,574	2,284	1,806	1,141
Government bonds	501	564	428	585
Other listed securities	559	591	580	555
Interbank placements	202	163	220	210
Total	**2,836**	**3,602**	**3,034**	**2,491**

Balance sheet encumbrance (unaudited)
The Group treats an asset as encumbered if it has been pledged or if it is subject to any form of arrangement to secure, collateralise or credit enhance any transaction from which it cannot be freely withdrawn. It is Group policy to maximise the amount of assets available for securitisation / pledging through the standardisation of loan structures and documentation.

At 31 December 2017 and 2016 the Group had the following encumbered assets.

Encumbered and unencumbered assets	**Encumbered[1] £m**	**Unencumbered £m**	**2017 Total £m**	Encumbered[1] £m	Unencumbered £m	2016 Total £m
Cash and balances with central banks	-	1,836	1,836	-	1,172	1,172
Mandatory deposits with central banks	1,206	17	1,223	1,157	21	1,178
Loans and advances to other banks	125	22	147	133	20	153
Loans and advances to banks - related party transactions	40	1,354	1,394	37	2,001	2,038
Loans and advances to customers	3,077	16,920	19,997	1,749	18,072	19,821
Available for sale financial assets	-	1,008	1,008	-	1,140	1,140
Other assets	-	630	630	-	458	458
Total assets	**4,448**	**21,787**	**26,235**	3,076	22,884	25,960
Encumbered cash and balances with central banks:						
Note cover[2]	1,172			1,121		
Cash ratio and other mandatory deposits	34			36		
	1,206			1,157		

Liquidity and funding risk monitoring
The Group's daily, weekly and monthly liquidity reporting (including a comprehensive suite of liquidity early warning signals) 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, including daily liquidity stress test results, are reported and reviewed by the Treasury, Finance and Risk functions and by the Group's senior management. These reports include a series of limits and triggers which, if triggered, are reported regularly to the ALCo. MI is reported to the ALCo, the ERC, the BRC and the Board.

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

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

During 2017 the Group has continued with the gradual replacement of gross flow cash hedging positions, as legacy placements and borrowings with the Parent expire. As a result the amounts due from and due to the Parent have changed from £2 billion and £1.9 billion, respectively at 31 December 2016, to £1.4 billion and £2.0 billion, respectively, at 31 December 2017.

[1] *Included in the encumbered assets at 31 December 2017 is £40 million (31 December 2016: £37 million) of collateral placed with the Parent in respect of derivative liabilities.*
[2] *Note cover relates to mandatory collateral with the Bank of England in respect of banknotes in circulation in Northern Ireland.*

2.2 Liquidity and funding risk (continued)

Contingent liquidity
The Group holds significant contingent liquidity collateral, comprised of mortgage-backed securities issued by Bowbell No 1 plc (refer to note 38), and raw loans pre-positioned in Bank of England facilities. This contingent liquidity collateral can be pledged against borrowings from central banks and other external market participants.

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.

The key drivers of ratings upgrades in 2017 were improving asset quality; longer record of stable profitability; strengthened capitalisation; and further reductions in the Bank's legacy commercial book.

Bank of Ireland UK ratings *(unaudited)*	**2017**	2016
Moody's	Baa2 stable outlook	Ba1 positive outlook
Fitch	BBB stable outlook	BBB- stable outlook

Maturity analysis of financial assets and liabilities
The following tables summarise the contractual maturity profile of the Group's financial assets and liabilities, at 31 December 2017 and 31 December 2016, 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 ISA 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 balances have been classified as fully accessible in the following table.

2017 Maturity analysis of financial assets and liabilities (discounted basis) *(unaudited)*	**Repayable on demand £m**	**0-3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Financial assets						
Cash and balances with central banks	1,836	-	-	-	-	1,836
Derivative financial instruments	2	5	5	14	1	27
Loans and advances to banks	147	1,223	-	-	-	1,370
Loans and advances to banks - related party transactions	434	-	275	668	17	1,394
Available for sale financial assets	-	121	111	763	13	1,008
Loans and advances to customers (before impairment provisions)	576	1,352	1,474	6,269	10,481	20,152
Total assets	**2,995**	**2,701**	**1,865**	**7,714**	**10,512**	**25,787**
Financial liabilities						
Deposits from banks	22	150	200	1,200	-	1,572
Deposits from banks - related party transactions	293	-	1,023	630	43	1,989
Customer accounts	14,085	1,951	2,396	529	-	18,961
Derivative financial instruments	-	5	5	43	12	65
Subordinated liabilities	-	-	-	-	290	290
Total liabilities	**14,400**	**2,106**	**3,624**	**2,402**	**345**	**22,877**
Net total assets and liabilities	(11,405)	595	(1,759)	5,312	10,167	2,910
Cumulative net assets and liabilities	**(11,405)**	**(10,810)**	**(12,569)**	**(7,257)**	**2,910**	**2,910**

2.2 Liquidity and funding risk (continued)

2016 Maturity analysis of financial assets and liabilities (discounted basis) *(unaudited)*	Repayable on demand £m	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Financial assets						
Cash and balances with central banks	1,172	-	-	-	-	1,172
Derivative financial instruments	-	18	10	7	20	55
Loans and advances to banks	174	1,157	-	-	-	1,331
Loans and advances to banks - related party transactions	447	48	448	1,077	18	2,038
Available for sale financial assets	-	75	123	889	53	1,140
Loans and advances to customers (before impairment provisions)	543	1,287	1,434	5,541	11,282	20,087
Total assets	2,336	2,585	2,015	7,514	11,373	25,823
Financial liabilities						
Deposits from banks	24	155	-	600	-	779
Deposits from banks - related party transactions	325	2	427	1,104	54	1,912
Customer accounts	12,904	2,590	3,163	818	-	19,475
Derivative financial instruments	-	11	7	71	13	102
Subordinated liabilities	-	-	-	-	335	335
Total liabilities	13,253	2,758	3,597	2,593	402	22,603
Net total assets and liabilities	(10,917)	(173)	(1,582)	4,921	10,971	3,220
Cumulative net assets and liabilities	(10,917)	(11,090)	(12,672)	(7,751)	3,220	3,220

2.3 Market risk

Key points:

- The Group does not engage in speculative trading for the purposes of making profits as a result of anticipation of movements in financial markets. Therefore, no discretionary risk is taken by the Group.
- During 2017, the Group continued to manage interest rate and foreign exchange exposure at acceptable levels, by seeking natural hedge solutions within the balance sheet and by hedging remaining exposures with the Parent as the hedge counterparty.

Definition *(audited)*
Market risk is the risk of loss arising from movements in interest rates, FX rates or other market prices. Market risk arises from the structure of the balance sheet and the Group's business mix and discretionary risk taking.

The Group recognises that the effective management of market risk is essential to the maintenance of stable earnings, the preservation of capital resources and the achievement of the Group's strategic objectives.

Market risk management *(audited)*
The management of market risk in the Group is governed by the Group's Risk Appetite Statement and by the Group Policy on Market Risk. The Group has an established governance structure for market risk that involves the Board, the BRC, the ERC, and the ALCo, which has primary responsibility for the oversight of market risk in the Group within the confines of the risk appetite set by the Board.

The Group has no risk appetite for the holding of proprietary market risk positions or the running of material open banking book market risk exposures. The Group, therefore, does not consider itself to have proprietary positions and hedges open banking book exposure to deminimus levels. However, the Group does have customer derivative foreign exchange 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 by hedging with the Parent. The overall market risk hedging approach is prioritised as follows;
(i) naturally hedge within the balance sheet;
(ii) execute derivative hedging contracts with the Parent; or
(iii) execute gross cash hedges.

Net derivative hedging was introduced by the Group in December 2013 and over time cash hedging deals with the Parent are being replaced by derivative contracts. Derivatives executed for hedging purposes are executed with the Parent only and are subject to ISDA and CSA standard documentation. Collateral requirements are calculated daily and posted as required. The Group uses derivative contracts with the Parent for hedging purposes only and seeks to apply hedge accounting where possible. The Group continues to maintain a deminimis limit for interest rate risk to reflect operational requirements only. This limit is monitored by the ALCo and approved by the Board. 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.

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. This has the effect of

2.3 Market risk (continued)

mitigating the impact of the interest rate cycle on the net interest margin.

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 and behavioural repricing 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.

In addition to this, the Group runs a series of stress tests, including parallel and non-parallel yield curve stress scenarios across all tenures, in order to further monitor and manage yield curve and repricing risk in the banking book.

The Group also applies market risk stress scenarios to manage and monitor the impact of stress events in relation to interest rate option risk, basis risk and net interest income sensitivity.

A dual purpose of the Group's market risk stress testing is to meet regulatory requirements and to ensure that appropriate capital is held by the Group.

The impact on the Group's economic value from an immediate and sustained 50 basis points shift, up or down, in the sterling yield curve applied to the banking book at 2017 and 2016, is shown below.

The sensitivity is indicative of the magnitude and direction of exposures but is based on an immediate and sustained shift of the same magnitude across the yield curve (parallel shift).

(audited)	**2017 £m**	2016 £m
+ 50 basis points	(0.16)	(0.28)
- 50 basis points	0.16	0.28

2.4 Regulatory risk

Key points:

- During 2017, supervisory bodies focused industrywide on the following key areas: business model and profitability risk, credit risk, impairment provisioning (IFRS 9), capital adequacy, business continuity management, recovery and resolution, and operational risk. In addition, new EU legislation which came into effect included the Market Abuse Regulation, 4th Money Laundering Directive and the Access to Payments Accounts Directive. Relevant UK legislation included treatment of PPI complaints, Payment Practices Regulations and PRA requirements on Buy to Let lending.
- Programmes continued / were established in the Group during 2017 to continue preparations for the significant regulatory change agenda to be implemented for 2018 and over the coming years, including:
  - Markets in Financial Instruments Directive / Markets in Financial Instruments Regulation: EU rules governing investment firms, trading venues and market structure, introducing new conduct of business obligations, trade reporting obligations and general obligations. Applicable from January 2018.
  - Payment Services Directive: EU rules including changes to information and transparency requirements on payments, new security requirements and faster handling of payments-related complaints. Applicable from January 2018.
  - General Data Protection Regulation: EU rules representing a fundamental change to the way firms must obtain consent for capture, process and storage of customer information. Applicable from May 2018.
  - Operational Continuity in Resolution: PRA requires banks to evidence they have the ability to continue providing services that support functions (core services) critical to the UK economy following a resolution event. Applicable from 1 January 2019.
- The heavy regulatory and compliance agenda is expected to continue in 2018. The Group will maintain its focus on continuing compliance with the existing and developing regulatory requirements of the EBA, FCA and PRA.
- Regulators conduct investigations and examinations on an industry wide basis from time to time.
- Engagement with the Group's regulators in 2017 included matters such as business model and profitability, cybersecurity, IT and third party sourcing risk, and credit risk across portfolios.
- The Competition & Markets Authority's (CMA) Open Banking requirements set a new digital standard that aims to give banking customers more control over their financial data by allowing them to share it with organisations other than their banks. On December 2017 the CMA issues directions for a number of banks extending the 13 January implementation date. For the Group, the implementation date was extended to 7 September 2018, and the Group is taking the appropriate steps to ensure compliance with the Direction issued by the CMA.

Definition
Regulatory risk is the risk of failure to meet new or existing regulatory and / or legislative requirements and deadlines or to embed requirements into processes.

The associated risk of regulatory change is the risk that a change in laws and regulations that govern the Group will materially impact the Group's business, profitability, capital, liquidity, products or markets; that the Group fails to take timely action; and/or that the Group fails to effectively manage the regulatory change process.

Risk management and measurement
The Group manages regulatory risk under its Risk Management Framework. The Framework identifies the Group's formal governance process around risk, including its framework for setting risk appetite and its approach to risk identification, assessment, measurement, management and reporting.

2.4 Regulatory risk (continued)

This is implemented by accountable executives and monitored by the R&ORC, the ERC, the BRC and Board in line with the overall risk governance structure outlined on pages 32 to 35. The effective management of regulatory risk is primarily the responsibility of business management and oversight is provided by Risk & Regulatory Affairs and Compliance & Conduct Risk functions. As detailed in the Group's RAS, the Bank has no appetite for failure to comply with its regulatory or legislative obligations. However, it acknowledges that instances may occur as a consequence of being in business.

The Bank has therefore established an approach to ensure the identification, assessment, monitoring, management and reporting of these instances.

Risk mitigation
Risk mitigants include the early identification, appropriate assessment and measurement and reporting of risks. The primary risk mitigants for regulatory risk are the existence of appropriate controls in place throughout the business and the effective planning and execution of regulatory change.

Risk reporting
The current status of regulatory risk is reported to senior executives and Board members through the Monthly Risk Report. The Head of Risk and Regulatory Affairs reports to the R&ORC on the status of regulatory risk in the Group, including the status of the top regulatory risks, the progress of risk mitigation plans, issues and breaches, and significant regulatory interactions.

2.5 Operational risk

Key points:

- The Group seeks to operate an effective framework for the mitigation and control of operational risk. During 2017 the Group continued to enhance its operational risk management processes, with more granular risk identification and assessment processes and alignment and integration of control mitigation tools which support increased utilisation of its technology solutions.
- A suite of improvement programmes to further develop the approach and application of risk management minimum standards for a number of material sub-classes of operational risk, were initiated in 2016, with delivery continued through 2017. This work will complete in 2018.
- In line with regulatory expections, the Group has continued their focus on overseeing the embedding and continuous enhancement of operational risk standards and practices. The Group actively engaged with regulatory bodies and continues to ensure it is in a position to meet its regulatory obligations.

Definition
Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events.

Risk management
The Group faces operational risks in the normal pursuit of its business objectives. The primary goals of operational risk management and assurance are ensuring the sustainability and integrity of the Group's operations and the protection of its reputation by controlling, mitigating or transferring the impact of operational risk.

Operational risk cannot be fully eliminated and it is the objective of the Group to manage operational risk within defined risk appetite measures, taking into account the cost of mitigation and the level of reduction in exposure which can be achieved.

The Group has an Operational Risk Management Framework (ORMF) which defines its approach to identifying, assessing, managing, monitoring and reporting the operational risks which may impact the achievement of the Group's business objectives. This framework consists of inter alia:

- formulation and dissemination of Group Operational Risk policies and policy standards specifying the risk management obligations of staff within the Group;
- establishment of organisational structures for the oversight, monitoring and management of operational risk throughout the Group; and
- embedding of formal operational risk management processes and standards within business and support units throughout the Group.

Operational risk policy
The Group's exposure to operational risk is governed by a suite of operational risk polices and policy standards approved by the R&ORC and managed in accordance with the Board approved risk appetite.

Risk mitigation and transfer
In addition to business unit risk mitigation initiatives, the Group implements specific policies and risk mitigation measures for key operational risks. Arrangements entered into with the Parent and third-party outsourced providers are governed through service level agreements which are monitored through formalised governance arrangements, KPIs, KRIs, risks, events and issues management. Outsourced service arrangements are subject to upfront and ongoing due diligence.

The Group calculates its Pillar I operational risk regulatory capital using the standard approach. The capital assigned to operational risk aims to ensure sufficient capital is held to cover the potential financial impact of severe but plausible operational risk events.

Operational risk events
An operational risk event is any occurrence that has caused, or is likely to cause, a financial, customer, regulatory or legal impact, or a business disruption.

All operational risk events (including

2.5 Operational risk (continued)

financial losses, near misses and instances of non-compliance) are recorded in the Group's operational risk repository, managed and reported on as appropriate.

A standard reporting threshold is used across the Group for inputs to Common Reporting (COREP) to the EBA and PRA.

Risk reporting
Regular operational risk updates including: the status of the top operational risks, the progress of associated risk mitigation initiatives; significant loss events; and the nature, scale and frequency of overall losses are reported to the R&ORC, the ERC, the BRC and the Board.

In addition to day-to-day control measures implemented by business units, theme-based monitoring of operational risks and controls is conducted throughout the year by an independent internal monitoring team within the Operational Risk & Financial Crime function. Such assurance activities provide a basis for assessment and validation of the performance of controls and the adequacy of mitigation.

2.6 Business and strategic risk

Key points:

- On an annual basis the Board reviews the Group's strategic objectives to confirm that the strategic shape and focus of the Group remains appropriate. Longer term viability is monitored through its ICAAP and 5-year planning processes.
- In 2017 the Group delivered a profit before tax of £151 million.
- Indicators of economic activity and business sentiment have recovered from their lows following the outcome of the UK referendum on EU membership but the macroeconomic environment remains challenging.

Definition
Business and Strategic Risk is defined as the risk of volatility to the Group's projected outcomes, including income statement and Balance Sheet impact and/or damage to the franchise, including that of the Group's joint ventures. It includes volatilities caused by changes in the competitive environment, new market entrants, new products or failure to develop and execute a strategy or anticipate or mitigate a related risk.

The risk may arise from a change in the competitive environment, new market entrants, new products, or a failure to anticipate or mitigate a related risk, and a breakdown / termination of a relationship with, or a significant underperformance of, a distribution partner.

Risk management, measurement and reporting
Business units are responsible for delivery of their business plans and management of such factors as pricing, business volumes, operating expenses and other factors that can introduce earnings volatility.

The Group reviews business and strategic risk as part of the annual risk identification process. The risk is measured quarterly, with a scorecard addressing movements in key indicators around income diversification, margin trends, customer advocacy, direct and indirect costs and staff turnover. Regular updates are provided to the ERC, the BRC and the Board.

Risk mitigation
The Group mitigates business risk through business planning methods, such as the diversification of revenue streams, cost base management and oversight of business plans which are informed by expectations of the external environment and the Group's strategic priorities.
At an operational level, the Group's annual budget process sets expectation at a business unit level for volumes and margins. The regular tracking of actual and forecast volumes and margins against budgeted levels, is a key financial management process in the mitigation of business risk.

Strategic risk is mitigated through its ICAAP and 5-year plan aswell as updates to the Board on industry developments, regular updates on the key macroeconomic environment impacting the Group's activities and a review of the competitive environment and strategies at both Group and business unit level.

The Group's Annual Strategy and Planning Process includes a review of the Group's business model.

Fluctuations in the prices in the used car market
Following the acquisition of Marshall Leasing Limited in November 2017, the Group's financial performance may now be affected by fluctuations in prices in the used car market. Such price fluctuations could also impact the Group's business, as it could affect the residual profitability of the vehicles at the end of leasing agreements. Marshall Leasing Limited operates an independent analysis tool to monitor this area and would seek to manage any exposure should the trend analysis predict it.

2.7 Reputation risk

Key points:

- The Group's reputation continues to be influenced and shaped by a range of factors including: macroeconomic and political environment, media, public and customer commentary and general sector developments. More specifically, the Group's decisions and actions in pursuit of its strategic and tactical business objectives and its interaction with the external environment will also influence its reputation.
- Throughout 2017, the Group continued to actively manage, measure and report on its reputation risk and to take this into account in its strategic decision making.

Definition
Reputation risk is defined as the risk to earnings or franchise value arising from adverse perception of the Group's image on the part of customers, partners, suppliers, counterparties, shareholders, investors, staff, legislators or regulators. This risk typically materialises through a loss of business in the areas affected. Reputation is not a standalone risk but overlaps with other risk areas and may often arise as a consequence of external events or operational risk related issues.

Risk management, measurement and reporting
Reputation risk indicators are monitored on an ongoing basis.

These indicators are:
- media monitoring;
- market trends and events;
- stakeholder engagement and monitoring; and
- risk events which may have the potential to impact the Group.

The Group reviews reputation risk as part of the annual risk identification process. Regular updates are reported to the ERC, the BRC and the Board.

Risk mitigation
A wide range of processes and structures are used to identify, assess and mitigate the potential risk to the Group's reputation. Managing the Group in a manner that ensures that the potential impact on the Group's reputation is taken into account in decision-making is paramount in mitigating against reputation risk.

2.8 Conduct risk

Key points:

- The Group recognises the importance of good conduct and is committed to placing customers at the heart of its strategic and operational decision-making.
- Throughout 2017, the FCA continued its focus on conduct risk standards and practices. The Group maintains constructive engagement with its supervisors and continues to ensure it is in a position to meet its regulatory obligations.
- In 2018, the Group will continue to embed, develop and enhance its conduct risk management tools and processes.

Definition
Conduct risk is the risk of failure to deliver a product or service in a manner reasonably expected by the Group's customers. Poor conduct or customer detriment can result from a failure in the Group's control framework, policies, processes, systems and controls, and / or its people. Such failure may also result in a breach of legislation, regulatory rules or principles including that of fairness.

Regulatory Environment
The Financial Conduct Authority's (FCA) priorities for 2018 will continue to influence the Group's agenda in both the short and medium term. The regulator's 2018 business plan includes work on a number of topics, which the Group has been working on. These matters include:

The FCA continues to focus on culture within regulated firms and requires senior management to ensure that regulated firms and their staff have an appropriate culture. On this basis it continues to see embedding of the Individual Accountability Regime (IAR) as a key tool to further its aim. The Group has taken steps in the past two years to embed the IAR and will continue to further refine its approach as the regulator publishes best practice, develops new prescribed responsibilities and makes other related pronouncements.

The regulator remains interested in how firms are making adequate arrangements to cater for the needs of vulnerable customers including ensuring they are treated fairly. The Group has a vulnerable customer programme in place which has taken steps to implement new arrangements in this area and continues to work on ensuring the Group meets related best practice, e.g. UK Finance best practice for bereaved customers.

A related matter identified through the regulator's work on vulnerability is the ability of customers to engage with financial services they need throughout their lifetime. The FCA considers that firms should be considering how best to provide access to financial services for customers who might otherwise be excluded from the financial services sector due to a diverse range of reasons, for example ageing population, firms' increased focus on digital transformation programmes and compliance reasons such as AML/CTF. The Group is continuing to consider what additional steps it can take to promote this area.

The regulator's 2017 work on customer understanding will continue to be an influence on the Group's work to ensure customers understand the products they buy before, during and after the point of sale. The Group is particularly cognisant of this work as it develops new products and is analysing customer feedback from new products launched in 2017 to further refine its approach in this area.

Risk management
The Group has no appetite for customer detriment and seeks to be fair, accessible

2.8 Conduct risk (continued)

and transparent in the provision of products and services to its customers at all times.

To ensure the Group's exposure to conduct risk is clearly defined, understood, measured, managed as appropriate and regularly reported upon, the Group has established a Conduct RMF which is underpinned by a set of clear, comprehensive and transparent measures supporting the conduct risk appetite statement.

The Group has developed an internal Customer Charter which provides a clear articulation of the Group's customer and partner commitments and is designed to place customers at the heart of its business. It is central to the Group's conduct risk culture which exists across the business and provides a common framework and lens for business decision-making, product design and customer operations, ensuring consistency across the Group. A Group conduct risk policy specifying the risk management obligations of management within the Group is in place.

The Group has in place an approach to vulnerable customers, which sets out desired outcomes and standards expected of business units and third party outsourced service providers in the treatment of those consumers that may be considered as vulnerable due to their personal circumstances and who are especially susceptible to detriment in the event that the Group does not act with the appropriate level of care.

This continues to be an important area of focus for the Group, with an emphasis on continually improving outcomes for vulnerable customers.

Conduct risk policy
The Group's exposure to conduct risk is governed by a policy approved by the BRC in accordance with the Board approved risk appetite and within the overall Group risk governance structure outlined on pages 32 to 35.

In addition to day-to-day control measures implemented by business units, monitoring of conduct risks and controls is conducted using a risk-based approach by an independent internal monitoring team within the Compliance and Conduct function.

Risk reporting
Each business unit in the Group produces a conduct risk scorecard aligned to the conduct risk appetite statement. These scorecards are reviewed by management and combined into an overall Conduct Risk Scorecard, which is used as the basis of onward reporting to the R&ORC, the ERC, the BRC and the Board.

3 Capital management

Key points:

- At all times during the financial year the Group maintained appropriate capital resources in line with regulatory requirements.
- CET 1 ratio is 14.7% at 31 December 2017 under both the CRD IV transitional and fully loaded basis.
- The Group will be required from 1 January 2018 to hold CET1 capital requirements of 8.4% comprising:
  - Pillar 1 4.5%, Pillar II (P2R) 2% and an additional 1.875% Capital Conservation Buffer.
  - This will increase to 8.9% in June and 9.4% in November with the phased implementation of 1% Countercyclical buffer by the FPC.
  - Pillar II Guidance (P2G) is not disclosed in accordance to regulatory preference.
- Sustained strong capital position enabled the payment of the equity dividend of £160 million to the Parent in October 2017 and repayment of £45 million subordinated debt in December 2017.
- The leverage ratio is 6.6% at 31 December 2017 under both the CRD IV transitional and fully loaded basis.

Capital adequacy risk
Capital adequacy risk is the risk that the Group holds insufficient capital to absorb extreme and unexpected losses, which could eventually result in the Group not being able to continue operating.

Capital management objectives and policies
The Group manages its capital position to ensure that it has sufficient capital to cover the risks of its business, support its strategy and to comply at all times with regulatory capital requirements.

Capital adequacy and its effective management is critical to the Group's ability to operate its businesses, grow organically and pursue its strategy. The Group's business and financial condition could be adversely affected if it is not able to manage its capital effectively or if the amount or quality of capital held is insufficient. This could arise in the case of 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 RWA and delays in the disposal of certain assets as a result of market conditions).

Capital requirements and capital resources
The Group complied with all its regulatory capital requirements throughout 2017.

The Group manages its capital resources to ensure that the overall amount and quality of resources exceeds the Group's capital requirements. Capital requirements are determined by the CRD IV, the CRR and firm specific requirements imposed by the PRA. The CRR minimum requirements are typically driven by credit risk, market risk and operational risk, and also require stress-absorbing buffers.

Additional firm-specific buffers reflect the PRA's view of the systemic importance of a bank and also internal capital adequacy which is determined by internal stress testing as part of the ICAAP.

An additional firm-specific countercyclical

3 Capital management (continued)

buffer is also required, reflecting the countercyclical buffer rates applicable to the exposures held by the Group.

Capital management reporting
The Group monitors and reports the capital position daily, monthly and quarterly. Reporting includes a suite of early warning triggers and measurement against risk appetite and is reviewed by the Prudential Risk team, the Capital Management Forum and the ALCo. The capital management information is reviewed by the ALCo, the ERC, the BRC and the Board.

Stress testing and capital planning
The Group uses stress testing as a key risk management tool to gain a better understanding of its risk profile and its resilience to internal and external shocks. In addition, stress testing provides a key input to the Group's capital assessments and related risk management and measurement assumptions.

The Group's stress testing is designed to:
- confirm the Group has sufficient capital resources;
- inform the setting of capital risk appetite measures;
- ensure the alignment between the Group's RMF and senior management decision making; and
- to provide sufficiently severe and forward looking scenarios.

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

The Group also undertakes reverse stress testing on an annual basis which informs, enhances and integrates with the stress testing framework by considering extreme events that could cause the Group to fail. This testing also improves risk identification and risk management and the results are also approved by the Board, as part of the Group's ICAAP. The Group's capital planning process includes a review of the Group's expected capital position which is reviewed and challenged on a monthly basis by senior management.

The Group's capital plan (which is approved at least annually by the Board) also includes sensitivities to ensure the continued resilience of the underlying assumptions under adverse conditions and changes to the regulatory landscape.

Details of the Group's equity are set out on the consolidated balance sheet on page 80.

Further detail of the Group's regulatory capital position, including ratios, are set out in section 1.7.12 of the Strategic report.

Group capital resources *(audited)*	**2017 £m**	2016 £m
Equity (including other equity reserves)	1,699	1,750
Other equity instruments	300	300
Dated subordinated loan capital	290	335
Total capital resources	**2,289**	**2,385**

Fully loaded - CRD IV	**2017 £m**	2016 £m
Common equity tier 1 capital ratio	14.7%	15.5%
Tier 1 capital ratio	17.7%	18.4%
Total capital ratio	20.5%	21.8%
Leverage ratio	6.6%	6.9%
Risk weighted assets (£m)	10,231	10,034

Governance

Directors and other information

Chairman
Mr. Robert Sharpe (N) (RE)

Non-executive Directors
Mr. Donal Collins
Ms. Susan Harris (A) (RI)
Mr. John Maltby (A) (RI) (N) (RE)
Ms. Mimi Kung (RI) (appointed 9 November 2017)

Executive Directors
Mr. Desmond Crowley
Mr. Neil Fuller
Mr. Thomas McAreavey

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

Company Secretary
Hill Wilson Secretarial Limited

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

Registered Number
07022885

Independent Auditors
PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Hays Galleria,
1 Hays Lane,
London,
SE1 2RD.

The Board of Directors

Robert Sharpe

Term of Office:
Appointed in
April 2016

Independent:
Yes

Chairman and Non-Executive Director
Appointed Chairman on the 27 April 2016, bringing over 35 years of Senior Executive and Board experience to the role, primarily in Retail Banking. He is currently Chairman at Al Rayan Bank plc, Honeycomb Investment Trust plc and Hampshire Trust Bank plc.

Robert worked extensively in the Middle East, where he held several Non-Executive Directorships at banks in the UAE, Oman and Turkey. Prior to this, he led the transformation and turnaround at West Bromwich Building Society as Chief Executive Officer, having formerly been Chief Executive at the Portman Building Society and Chief Executive of Bank of Ireland's business in the UK. His previous Non-Executive Director roles include Barclays Bank Pension Board, Chairman of Vaultex (UK) Ltd, George Wimpey plc, LSL Properties plc and the RIAS Group Ltd.

External Appointments:
Chairman and Non-executive Director of Al Rayan Bank.
Chairman and Non-executive Director of Honeycomb Investment Trust Ltd.
Chairman and Non-executive Director of Hampshire Trust Bank.

Desmond Crowley

Appointed:
Appointed in
September 2009

Independent:
No

Chief Executive Officer, Retail UK Division
Appointed Director of Bank of Ireland (UK) plc in September 2009. Appointed Chief Executive Officer of Bank of Ireland (UK) plc in March 2012. Joined BoI Group in 1988. In March 2000 became a member of the Bank of Ireland 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.

Previously Chairman of Post Office Financial Services. A Director of First Rate Exchange Services Limited, the foreign exchange joint venture with UK Post Office. He is also Director of New Ireland Assurance Company plc.

External Appointments:
None

Neil Fuller

Term of Office:
Appointed in
October 2015

Independent:
No

Chief Risk Officer
Appointed Director of Bank of Ireland (UK) plc and Chief Risk Officer in October 2015. Neil joined Bank of Ireland from GE Capital UK, where he held the role of Chief Risk Officer since 2011. He has over 30 years of financial services experience, having previously worked for Royal Bank of Scotland & NatWest, where he held the role of Chief Risk Officer, UK Retail Division, and having previously held a number of senior management roles in UK Retail Banking across Credit Risk, Enterprise & Operational Risk and Operations. Neil is also a Director of First Rate Exchange Services Limited, the foreign exchange joint venture with the UK Post Office.

External Appointments
None

Directors and other information (continued)

Thomas McAreavey

Term of Office:
Appointed in
March 2017

Independent:
No

Chief Financial Officer
Appointed Director of Bank of Ireland (UK) plc and Chief Financial Officer in March 2017. He has over 15 years' experience in the Bank of Ireland Group, having held various senior management positions within Finance, including leading a range of strategic projects for BoI. Prior to that he held a management position within Pricewaterhouse Coopers LLP. He is a Fellow Chartered Accountant.
Thomas is also a Director of a number of BoI Group subsidiaries.

External Appointments
None

Donal Collins

Term of Office:
Appointed in
July 2015

Independent:
No

Head of Group Strategy & Development
Appointed Director of Bank of Ireland (UK) plc in July 2015. Donal joined Bank of Ireland Group in 1999 and became a member of the Group Executive Committee in 2014. He has held a number of senior management positions including Director, Corporate Banking; Head of Group Projects and Head of Group Strategy Development. Prior to joining Bank of Ireland, Donal worked for KBC Bank in a range of international senior management roles in aerospace, infrastructure and asset financing and KPMG Ireland as Director, Taxation. Donal is a graduate of University College Dublin. He is a Fellow of Chartered Accountants of Ireland and an Associate of the Irish Institute of Taxation.

External Appointments
None

Susan Harris, BSc (Hons), ACMA

Term of Office:
Appointed in
July 2015

Independent:
Yes

Non-Executive Director
Appointed Director of Bank of Ireland (UK) plc in July 2015, and member of the Audit and Risk Committees. Sue was previously a non-executive director of St James's Place, Chair of the Finance and Audit Committees at Mencap, and Chair of Trustees of KCP Youth. She has held a number of senior executive positions in the financial services and retail sectors, including Group Audit Director, Lloyds Banking Group (LBG), Financial Control Director, LBG, Finance Director of LBG's Retail Bank; and Finance Director of Cheltenham & Gloucester. Sue has held a number of other senior finance executive positions including Managing Director Finance at Standard Life, and Head of Corporate Development and Group Treasurer of Marks & Spencer. Sue is Chair of the Audit and Assurance Council of the Financial Reporting Council and a member of the Codes and Standards Committee.

External Appointments
Non-executive Director and chair of the Audit and Risk Committee of Abcam
Non-executive Director at Schroder & Co.
Non-executive Director at Barclays Pension Fund Trustees Limited

Directors and other information (continued)

John Maltby
BSc (Hons)

Term of Office:
Appointed in
November 2015

Independent:
Yes

Non-Executive Director
Appointed to the Board of Bank of Ireland (UK) plc in November 2015, and appointed Chair of the Risk Committee in August 2017. John is also interim Chair of the Audit Committee and a member of the Nomination and Remuneration Committees. John is currently Chairman of Good Energy Group plc, and a member of its Audit and Remuneration Committees. Previous Board appointments include CEO and member of Transitional Board of Williams & Glynn, Chairman of Board of Lloyds Commercial Finance, Member of the Board Cheltenham & Gloucester plc, Chairman of the Board of Start Mortgages Ireland, and Member of the Board of Lombard Bank. He has also previously been Group Chief Executive of Kensington Group PLC, a specialist mortgage business and Group Director, Commercial Banking for Lloyds Banking Group. John has also held senior executive roles throughout the financial services industry, including NatWest Group PLC, Barclays Bank PLC and Abbey National PLC.

External Appointments
Chairman and Non-executive Director of Good Energy Group plc
Non-executive Director at NCS Trust CIC

Mimi Kung

Term of Office:
Appointed in
November 2017

Independent:
Yes

Non-Executive Director
Appointed as Director of Bank of Ireland (UK) plc in November 2017. Member of the Risk Committee. Mimi attended the Boston University School of Management (1998) and Oxford University (2003). Mimi has held various senior positions at American Express since 1995 including that of Chief Financial Officer of American Express Europe and, most recently, that of Senior Vice-President, Head of the "Card Services Central Europe & International Currency Cards" function, and country manager for Italy.

External Appointments
Non-executive Director at Poste Italiane

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 2017. 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 66 to 69. The Group's structure is set out in the strategic report in section 1.3 and the future developments of the Group are incorporated in the strategic report in section 1.5.

Principal activities
The Bank is an 'authorised institution' under the Financial Services and Markets Act 2000 and is regulated by the FCA and the 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 for the year ended 31 December 2017 was £130 million (year ended 31 December 2016: £164 million profit). There was no profit or loss attributable to non-controlling interests for the year ended 31 December 2017 (year ended 31 December 2016: £nil). An analysis of performance is set out in the strategic report on pages 5 to 29.

Dividends
On 18 October 2017 a dividend payment of £160 million was paid to the Parent.

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

- Pat Butler, Non-executive, 10 January 2017;
- Thomas McAreavey, Executive, 2 March 2017; and
- Mimi Kung, Non-executive, 9 November 2017.

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

- Peter Shaw, Non-executive, 31 July 2017;
- David Weymouth, Non-executive, 30 November 2017;
- Pat Butler, Non-executive, 31 December 2017; and
- Lewis Love, Non-executive, 23 February 2018.

Corporate governance
It is the Group's policy not to include the disclosures in respect of the 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 ultimate parent is Bank of Ireland Group plc. The Consolidated Annual Report of Bank of Ireland Group plc details the Corporate Governance framework applicable to the Group and its subsidiaries. Bank of Ireland Group plc 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.

Further details on the Group's commitment to corporate social responsibility can be found in section 1.6 of the strategic report.

Risk management
The Group's principal risks and uncertainties are discussed in the strategic report on pages 24 to 29.

Additional risk disclosures for the Group can be found in the Risk Management section.

Employees
For the year ended 31 December 2017, the Group had an average of 277 direct employees (for the year ended December 2016: 177 direct employees) and 438 employees (for the year ended 31 December 2016: 328 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 recruitment and employment practices, the Group does not discriminate against individuals on the basis of any factor which is not relevant to performance including an individuals' sex, race, colour, disability, sexual orientation, marital status or religious beliefs.

The Group has a number of programmes to support colleagues who become disabled or acquire a long-term health condition.

To support continued employment and training, career development and promotion of all employees, 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 2017 or in the year ended 31 December 2016.

Voting Rights
Voting at any general meeting is by a show of hands or by poll. The Annual General Meeting of the Group is scheduled to take place on 1 May 2018, and a copy of the Notice of the Meeting will be available on the Group's website when it is issued. The Group is a wholly owned subsidiary of the Governor and Company of the Bank of Ireland. Details of the Parent's shareholding can be found in the Notes to the Accounts in note 31.

Going concern
The Directors have considered the appropriateness of the going concern basis in preparing the financial statements, for the year ended 31 December 2017, on page 85 which forms part of the Report of the Directors.

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 39 to the consolidated financial statements.

Financial Statements

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. In accordance with that law, the Directors have prepared the Group's and the Bank's financial statements, in accordance with IFRS and IFRS Interpretations Committee (IFRS IC) interpretations as adopted by the European Union (EU).

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 the Bank and of the profit or loss of the Group and Bank 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 IFRS, as adopted by the EU, 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 Bank'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, and as regards the Group financial statements, Article 4 of the IAS Regulation.

They are also responsible for safeguarding the assets of the Bank and 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 of the Companies Act 2006, 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.

Change of auditors
A competitive external audit tender process, overseen by Bank of Ireland Group plc Audit Committee was conducted in 2017 and the appointment of KPMG as Group External Auditors will be recommended to shareholders for approval at the Group's 2018 Annual General Meeting, subject to which KPMG will conduct the Group's audit for the year ended 31 December 2018.

As approved by the Board and signed on its behalf by:

Thomas McAreavey
Director
6 March 2018

Company Number: 07022885

Independent auditors' report to the members of Bank of Ireland (UK) plc

Report on the audit of the group financial statements

Opinion

In our opinion, Bank of Ireland (UK) plc's group financial statements (the "financial statements"):

- give a true and fair view of the state of the group's affairs as at 31 December 2017 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.

We have audited the financial statements, included within the Annual Report, which comprise: the consolidated balance sheet as at 31 December 2017; the consolidated income statement and consolidated statement of other comprehensive income, the consolidated cash flow statement, and the consolidated statement of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the group.

Other than those disclosed in note 8 to the financial statements, we have provided no non-audit services to the group in the period from 1 January 2017 to 31 December 2017.

Our audit approach

Overview

- Overall group materiality: £7,600,000, based on 5% of profit before tax. The group is profit orientated and profit before tax is one of the key metrics used to assess its performance.
- The scope of our audit and the nature, timing and extent of the audit procedures performed were determined by our risk assessment, the financial significance of the group's reporting components and other qualitative factors.
- We performed full scope audit procedures over components considered to be financially significant. We also performed audit procedures over specific account balances in other components that were significant to the group.
- PwC Ireland were essential to this scope carrying out the majority of the audit procedures relating to a number of areas including IT testing and IFRS 9 transition.
- Audit coverage for individual line items within the consolidated income statement and consolidated balance sheet falls in the range of 79% to 100%; most line items have coverage above 90%.
- See page 76 for further details.
- Impairment provision on loans and advances to customers including IFRS 9 transition.
- Revenue recognition relating to effective interest rate (EIR) accounting for mortgages and unwind of fair value adjustments on acquired mortgages.
- IT risk.

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

We gained an understanding of the legal and regulatory framework applicable to the group and the industry in which it operates, and considered the risk of acts by the group which were contrary to applicable laws and regulations, including fraud. We designed audit procedures at group and significant component level to respond to the risk, recognising that the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. We focused on laws and regulations that could give rise to a material misstatement in the group and company financial statements, including, but not limited to, the Companies Act 2006, the Financial Services and Markets Act 2000 and UK tax legislation. Our tests included, but were not limited to, review of the financial statement disclosures to underlying supporting documentation, review of correspondence with the regulators, enquiries of management and review of significant component auditors' work. There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it.

Our audit approach (continued)

We did not identify any key audit matters relating to irregularities, including fraud. As in all of our audits we also addressed the risk of management override of internal controls, including testing journals and evaluating whether there was evidence of bias by the directors that represented a risk of material misstatement due to fraud.

Key audit matters

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

Key audit matter	How our audit addressed the key audit matter
Impairment provision on loans and advances to customers including IFRS 9 transition Refer to pages 85 to 98 (Group Accounting Policies), page 97 (Critical accounting estimates and judgments), and pages 100 to 131 (Notes to the Consolidated Financial Statements). We focused on the identification and determination of provisions in relation to the mortgage and commercial loan portfolios as it requires management to make complex and subjective judgments. In the commercial loan portfolio, individual impairment assessments are performed where there are observed impairment indicators. There is significant judgement required for each loan to determine the level of any provision. Our focus was on the principal assumptions applied by management in estimating the impairment allowance such as the value of collateral and forecast cash flows. For the incurred but not reported (IBNR) and collective specific mortgage provisions we focused on: • The appropriateness of the models used to estimated impairment provisions; • The judgements around the propensities of default and subsequent possession which are based on historic data and customer credit profiles; and • Loss rates determined by expected recoveries focusing on management's assumptions around house price changes and forced sale discounts. IAS 8 requires the Group to disclose the impact of the adoption of IFRS 9 (which is effective for accounting periods beginning on or after 1 January 2018). We consider this to be a key audit matter because new models have been developed to calculate IFRS 9 impairment losses (see pages 53 to 55) and judgement is required in a number of significant areas in relation to the calculation of Expected Credit Loss.	We understood and evaluated the design of key controls over the commercial and mortgage impairment processes and tested their effectiveness. We noted no significant exceptions in these controls. Accordingly, we relied on them for the purposes of our audit. In addition, we performed the substantive procedures described below. *Commercial impairment* For a sample of individually impaired loans, we evaluated the specific circumstances of the borrower, the basis on which the provision was determined and whether key judgements were appropriate. We re-performed management's discounted cash flow forecast calculations, testing key inputs such as expected future cash flows and discount rates. We tested the valuation of collateral held and challenged management on subjective estimates and assumptions. We also compared gains and losses realised when a loan is sold or exited to the existing provision. Based on the procedures performed and the evidence obtained, we found management's methodology, assumptions and judgments to be reasonable. *Mortgage impairment* We assessed the appropriateness of key assumptions used in the modelling by comparing against recent group experience as well as our industry experience. We tested the completeness and accuracy of underlying data sources into the impairment models. We reviewed the coding used in the model for the calculation of the provisions and the calculation of key model inputs. We performed sensitivity analyses in order to identify higher risk assumptions and inputs which included default and possession propensities and loss rates. In these areas we performed additional targeted procedures and we concluded that the assumptions and inputs used were reasonable. *IFRS 9* Due to the structure of the Bank of Ireland Group's IFRS 9 programme, key IFRS 9 transition processes and controls were operated in Dublin and as such, the majority of the audit procedures relating to IFRS 9 transition were performed by PwC Ireland, in Dublin. We remained responsible for ensuring appropriate audit procedures were performed, as well as the reporting of findings and results to the Group. In respect of the disclosure for the impact of IFRS 9, we obtained an understanding of and evaluated management's process for the calculation of the transition adjustment including governance over the determination of key judgements. We read key technical papers prepared by management during the transitions project as part of our assessment of the effectiveness of the implementation. We tested the controls developed by management for the purpose of generating the transition adjustment for both Impairment and Classification & Measurement. With the assistance of PwC specialists we tested key IFRS 9 models developed by management where these were relevant to the calculation of the transition adjustment. We challenged the reasonableness and appropriateness of key assumptions and judgements made by management. We also considered the output of the Classification & Measurement work stream for consistency with our understanding of the group's business models. Finally, we considered management's rationalisation of the overall calculated impact of IFRS9 on the Balance Sheet position at 1 January 2018. We concluded that the group's process for estimating the transition adjustment including the selection of assumptions and evaluation of model outputs was reasonable. We consider that the disclosures reflect the circumstances of the group and the requirements of IAS 8.

Our audit approach (continued)

Key audit matter	How our audit addressed the key audit matter
Revenue recognition relating to effective interest rate (EIR) accounting for mortgages and unwind of fair value adjustments on acquired mortgages Refer to pages 85 to 98 (Group Accounting Policies), page 98 (Critical accounting estimates and judgments), and pages 100 to 131 (Notes to the Consolidated Financial Statements). The group's total loans and advances to customers balance of £20 billion and net interest income of £471 million include certain manual adjustments that involve management judgment. The vast majority of the group's income is system generated and requires minimal judgment, therefore we focused our work in relation to the risk of fraud in revenue recognition on adjustments relating to mortgage EIR and the unwind of fair value adjustments linked to the acquisition of mortgages. Changes in the assumptions used in the associated models could have a material impact on the revenue recognised in any one accounting period. We focused on the most significant judgment for mortgage EIR which is the estimation of the expected life of the mortgage over which the associated fees, costs and discounts are spread. In relation to the unwind of fair value adjustments linked to acquired mortgages, we focused on significant judgment management make in assessing rates of future customer redemptions, particularly relating to buy-to-let mortgages.	Across both the mortgage EIR and fair value unwind models, we tested controls over the assumptions used and checked the accuracy of model calculations by reviewing formulas used and considering whether these were in line with our expectations. For mortgage EIR we: • substantively tested a sample of fees, costs and interest rates back to underlying lending agreements and source documentation; • assessed the estimate of the expected mortgage life applied and forecast cash flows during this life by comparing to recent group experience and expectations of future patterns For fair value unwind we: • tested the accuracy of data inputs into the model; • agreed redemption assumptions applied in the model to those that were approved by management and considered the reasonableness of the assumptions. We evaluated whether the disclosures made in the financial statements were sufficiently clear in describing the key assumptions and their sensitivity. We concluded that whilst there is significant judgment inherent in the mortgage EIR and fair value unwind adjustments, the assumptions applied were within a reasonable range based on past experience and future assumptions. We concluded the disclosures provided appropriate detail of the estimation uncertainty and the impact of actual future customer experience differing from the assumptions made.

Our audit approach (continued)

Key audit matter	How our audit addressed the key audit matter
IT risk The Group has a complex IT environment and operates a number of IT applications to support its business activities. A significant number of these applications (whether developed by management or purchased from third party vendors) have been in place for many years. There is a mix of automated and manual interfaces between applications. The IT control framework over financial reporting includes standardised IT general controls most of which relate to a number of applications, designed to prevent or detect material misstatements in the recording, processing and reporting of financial information. The Group invests to maintain the operating effectiveness of the IT systems as well as managing other factors including increased expectations from regulators and customers. Bank of Ireland Group Internal Audit ("GIA") has reported on the related internal control and operational risk considerations. Management has an ongoing risk management programme in place to identify, rate, mitigate and report on risk including IT and Operational risk considerations. We focused on this area because the Group's business is highly IT dependent, the IT environment is complex and the design and operating effectiveness of IT controls and of IT risk mitigants supports the financial reporting process.	Due to the structure of the Bank of Ireland Group, the key IT processes are based in Dublin and as such, the majority of the audit work was performed by PwC Ireland, in Dublin. We remained responsible for the overall scoping of the audit work, as well as the reporting of findings and results relevant to the Group. Throughout the audit relevant findings identified by PwC Ireland were reported to us so we could determine the impact on our audit approach and opinion. Using principally PwC Ireland IT audit specialists, we updated our understanding of the Group's IT environment and of changes made to it during 2017. In particular, we considered the outputs from management's IT risk management process and the findings of reviews conducted by GIA. We considered the impact of the assessed risks on our audit approach. We considered those IT risks and significant GIA IT audit issues that management assessed as relevant to financial reporting and tested and challenged management's assessment of the mitigation of these risks relevant to financial reporting. We also considered management's documentation and testing of the design and operating effectiveness of the IT controls within the Bank of Ireland Group's Internal Control Framework over financial reporting and tested the design and operating effectiveness of those controls upon which we wished to rely. Where relevant, we considered whether compensating controls acted as effective mitigants of design or operating deficiencies identified by management or us. In the absence of sufficient compensating controls, we examined, tested and challenged management's documented assessments of the risk which control deficiencies posed to the financial reporting process. We concluded following completion of our audit procedures that management's assessments of the impact of IT risk matters on the financial reporting process were reasonable and that we could place reliance on the operation of in-scope IT systems and reports generated from them.

Our audit approach (continued)

How we tailored the audit scope
We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the group, the accounting processes and controls, and the industry in which it operates.

The group comprises twenty components through which it reports its operating results and financial position of which four are significant to our audit. These are Mortgages, Business Banking, Post Office Financial Services and Divisional Centre. The components report through an integrated consolidation system. We identified the components which, in our view, required a full scope audit either due to their size or their risk characteristics in the context to the group's consolidated financial statements.

In order to achieve the desired level of audit evidence on each account balance in the financial statements, we identified nine further reporting units that we determined to be individually significant in respect of one or more account balances and performed specific audit procedures over those account balances. Specific audit procedures were performed on credit cards, ATM income and expense and pension assets and liabilities.

We used component PwC auditors operating under our instructions who are familiar with the relevant businesses to audit specific reporting units. Where the work was performed by component auditors, we determined the level of involvement we needed to have in their work to be able to conclude whether sufficient audit evidence had been obtained.

Processes supporting the group's operations are also performed at a Bank of Ireland Group plc level in the Republic of Ireland, including the hosting and monitoring of the IT systems used by the group. As part of the planning and execution of the audit, we visited the auditor of the parent, held regular physical and telephone meetings throughout the audit and reviewed extracts from PwC Ireland's audit file to corroborate that the procedures performed on our behalf were sufficient for our purposes.

Together with additional procedures performed at the Group level, this gave us the evidence we needed for our opinion on the financial statements as a whole.

Audit coverage for individual line items within the consolidated income statement and consolidated balance sheet falls in the range of 79% to 100%; most line items have coverage above 90%.

Materiality
The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Bank of Ireland (UK) financial statements
Overall Group materiality £7.6 million
How we determined it 5% of profit before tax.
Rationale for benchmark applied Based on the benchmarks used in the annual report, profit before tax is a key measure used by the shareholders in assessing the performance of the group, and is a generally accepted auditing benchmark.

Our audit approach (continued)

For each component in the scope of our group audit, we allocated a materiality that is less than our overall group materiality. The range of materiality allocated across components was between £550,000 and £6,200,000. Certain components were audited to a local statutory audit materiality that was also less than our overall group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £375,000 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern

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

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

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's ability to continue as a going concern.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Report of the Directors, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, ISAs (UK) require us also to report certain opinions and matters as described below.

Strategic Report and Report of the Directors

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Report of the Directors for the year ended 31 December 2017 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the group and its environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Report of the Directors.

Responsibilities for the financial statements and the audit

Responsibilities of the Directors for the financial statements
As explained more fully in the Statement of Directors' Responsibilities set out on page 71, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or to cease operations, or have no realistic alternative but to do so.

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

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report
This report, including the opinions, has been prepared for and only for the company'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.

Other required reporting

Companies Act 2006 exception reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion:
- we have not received all the information and explanations we require for our audit; or
- certain disclosures of directors' remuneration specified by law are not made.

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the audit committee, we were appointed by the directors on 9 July 2010 to audit the financial statements for the period ended 31 March 2010 and subsequent financial periods. The period of total uninterrupted engagement is 7.5 years, covering the periods ended 31 March 2010 to 31 December 2017.

Other matter

We have reported separately on the company financial statements of Bank of Ireland (UK) plc for the year ended 31 December 2017.

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

6 March 2018

Consolidated Financial Statements

Consolidated income statement *(for the year ended 31 December 2017)*

	Note	2017 £m	2016 £m
Interest income	2	651	762
Interest expense	3	(180)	(265)
Net interest income		**471**	**497**
Fee and commission income	4	114	118
Fee and commission expense	4	(115)	(121)
Net trading expense	5	(1)	(6)
Other operating income	6	2	6
Total operating income		**471**	**494**
Operating expenses	7	(328)	(313)
Operating profit before impairment charges on financial assets		**143**	**181**
Impairment charges on financial assets	9	(26)	(23)
Operating profit		**117**	**158**
Share of profit after tax of joint venture	10	34	35
Profit before taxation		**151**	**193**
Taxation charge	11	(21)	(29)
Profit for the year		**130**	**164**

Consolidated statement of other comprehensive income *(for the year ended 31 December 2017)*

	Note	2017 £m	2016 £m
Profit for the year		**130**	**164**
Items that may be reclassified to profit or loss in subsequent periods			
Net change in cash flow hedge reserve (net of tax)[1]		(9)	21
Net change in available for sale reserve (net of tax)[2]		-	3
Total items that may be reclassified to profit or loss in subsequent periods		**(9)**	**24**
Items that will not be reclassified to profit or loss in subsequent periods			
Net actuarial gain / (loss) on defined benefit schemes[3]	28	6	(3)
Net change in revaluation reserve, net of tax		1	-
Total items that will not be reclassified to profit or loss in subsequent periods		**7**	**(3)**
Other comprehensive (expense) / income for the year, net of tax		**(2)**	**21**
Total comprehensive income for the year, net of tax		**128**	**185**

[1] *Net of tax credit £3 million (2016: charge £7 million).*
[2] *Net of tax £0.4 million (2016: £1 million).*
[3] *Net of tax £1 million (2016: £1 million).*

Consolidated balance sheet *(as at 31 December 2017)*

	Note	2017 £m	2016 £m
Assets			
Cash and balances at central banks	12	1,836	1,172
Items in the course of collection from other banks		192	131
Derivative financial instruments	13	27	55
Loans and advances to banks	14	2,764	3,369
Available for sale financial assets	15	1,008	1,140
Loans and advances to customers	16	19,997	19,821
Interest in joint venture	18	61	61
Intangible assets	19	61	25
Property, plant and equipment	21	104	8
Other assets	22	106	109
Deferred tax assets	23	71	69
Retirement benefit asset	28	8	-
Total assets		**26,235**	**25,960**
Equity and liabilities			
Deposits from banks	24	3,561	2,691
Customer accounts	25	18,961	19,475
Items in the course of transmission to other banks		108	85
Derivative financial instruments	13	65	102
Other liabilities	26	1,233	1,200
Provisions	27	13	16
Current tax liability		5	6
Subordinated liabilities	29	290	335
Total liabilities		**24,236**	**23,910**
Equity			
Share capital	31	851	851
Retained earnings		254	296
Other reserves		594	603
Other equity instruments	32	300	300
Total equity attributable to owners of the Bank		**1,999**	**2,050**
Total equity and liabilities		**26,235**	**25,960**

The financial statements on pages 79 to 131 were approved by the Board on 6 March 2018 and were signed on its behalf by:

Thomas McAreavey

Thomas McAreavey
Director
6 March 2018

Company Number: 07022885

Consolidated statement of changes in equity *(for the year ended 31 December 2017)*

	Note	2017 £m	2016 £m
Share capital			
Balance at 1 January		851	851
Balance at 31 December		**851**	**851**
Retained earnings			
Balance at 1 January		296	374
Profit for the year attributable to equity holders of the Bank		130	164
Dividend on ordinary shares		(160)	(220)
Distribution on other equity instruments - Additional tier 1 coupon, net of tax[1]		(18)	(19)
Remeasurement of the net defined benefit pension liability		6	(3)
Balance at 31 December		**254**	**296**
Other equity instruments			
Balance at 1 January		300	300
Balance at 31 December		**300**	**300**
Other reserves:			
Available for sale reserve			
Balance at 1 January		5	2
Changes in fair value, net of hedge accounting adjustments		(1)	9
Transfer to income statement (pre tax)		-	(5)
Deferred tax on reserve movements		-	(1)
Balance at 31 December		**4**	**5**
Revaluation reserve - property			
Balance at 1 January		-	-
Revaluation of property		1	-
Balance at 31 December		**1**	**-**
Cash flow hedge reserve			
Balance at 1 January		32	11
Changes in fair value		3	43
Transfer to income statement (pre tax)		(15)	(15)
Deferred tax on reserve movements		3	(7)
Balance at 31 December		**23**	**32**
Capital contribution			
Balance at 1 January		266	266
Balance at 31 December		**266**	**266**
Capital redemption reserve fund			
Balance at 1 January		300	300
Balance at 31 December		**300**	**300**
Total other reserves		**594**	**603**
Total equity		**1,999**	**2,050**
Included in the above:			
Total comprehensive income attributable to owners of the Bank		128	185
Total comprehensive income for the year		**128**	**185**

[1] *The Additional tier 1 coupon paid to the Parent of £18 million (2016: £19 million) is presented net of the related tax credit of £6 million (2016: £5 million), comprising £5 million (2016: £3 million) relating to current tax and £1 million (2016: £2 million) relating to deferred tax.*

Consolidated cash flow statement *(for the year ended 31 December 2017)*

	Note	2017 £m	2016 £m
Cash flows from operating activities			
Profit before taxation		151	193
Interest expense on subordinated liabilities and other capital instruments	3	24	24
Depreciation and amortisation	7,15, 21	11	10
Impairment charges on loans and advances to customers	9	26	23
Share of results of joint venture	10	(34)	(35)
Net change in prepayments and interest receivable	22	6	11
Net change in accruals and interest payable	26	(24)	(43)
Charge for provisions	27	11	12
Other non-cash items		20	13
Cash flows from operating activities before changes in operating assets and liabilities		**191**	**208**
Net change in items in the course of collection to / from banks		(38)	27
Net change in derivative financial instruments		(4)	17
Net change in loans and advances to banks		571	676
Net change in loans and advances to customers		(217)	(576)
Net change in deposits from banks		800	85
Net change in customer accounts		(514)	(2,098)
Net change in provisions		(14)	(9)
Net change in retirement benefit obligation		(2)	(2)
Net change in other assets and other liabilities		46	80
Net cash flow from operating assets and liabilities		**628**	**(1,800)**
Net cash flow from operating activities before taxation		**819**	**(1,592)**
Taxation paid		(14)	(10)
Net cash flow from operating activities		**805**	**(1,602)**
Investing activities (section (a) - see next page)		89	(134)
Financing activities (section (b) - see next page)		(253)	(268)
Net change in cash and cash equivalents		**641**	**(2,004)**
Opening cash and cash equivalents		2,999	5,003
Closing cash and cash equivalents	12	**3,640**	**2,999**

Consolidated cash flow statement *(for the year ended 31 December 2017) (continued)*

	Note	**2017 £m**	2016 £m
(a) Investing activities			
Acquisition of a subsidiary, net of cash acquired	20	(41)	-
Additions to available for sale financial assets	15	(82)	(301)
Redemptions and disposals of available for sale financial assets	15	198	133
Dividends received from joint venture	18	34	35
Additions to intangible assets	19	(1)	(1)
Additions to property, plant and equipment	21	(19)	-
Cash flows from investing activities		**89**	**(134)**
(b) Financing activities			
Dividend paid on ordinary shares	36	(160)	(220)
Additional tier 1 coupon paid	36	(24)	(24)
Interest paid on subordinated liabilities	3	(24)	(24)
Repurchase of subordinated liabilities	29	(135)	-
Issue of subordinated liabilities	29	90	-
Cash flows from financing activities		**(253)**	**(268)**

Group Accounting Policies

Accounting policies

The following are the principal accounting policies for the Bank of Ireland (UK) plc Group and Bank. These policies have been consistently applied to all the years presented, unless otherwise stated.

Basis of preparation

These financial statements are the consolidated financial statements of the Bank of Ireland (UK) plc and its subsidaries (collectively the 'Group'), and the separate financial statements of the Bank.

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 cash flow statement, 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, 2.3 and 3 of the Risk Management Report, that are described as being an integral part of the financial statements. The Consolidated financial statements comprise the Bank and its controlled entities, as per note 38.

The separate financial statements of the Bank reflect the financial position of the Bank only and do not consolidate the results of any subsidiaries.

The consolidated financial statements of the Group are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS and with the European Union (Credit Institutions: Financial Statements) Regulations, 2015.

The financial statements of the Bank are prepared under FRS 101 'Reduced disclosure framework' and in accordance with the Companies Act 2006. In preparing these financial statements the Bank applies the recognition, measurement and disclosure requirements of IFRS as adopted by the EU. The Bank has applied the exemptions available under FRS 101 in respect of the following disclosures:

- statement of Cash Flows;
- disclosures in respect of transactions with wholly-owned subsidiaries;
- certain requirements of IAS 1 'Presentation of financial statements'; and
- the effects of new but not yet effective IFRSs.

The financial statements have been prepared on the going concern basis, in accordance with IFRS and IFRS IC interpretations, as adopted for use in the EU 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 or FRS 101 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 97 and 98.

Adoption of new accounting standards

The following new amendments have been adopted and consistently applied by the Group during the year ended 31 December 2017:

- IAS 7 'Statement of cash flows': Disclosure Initiative narrow-scope amendments; and
- IAS 12 'Income taxes': Recognition of Deferred Tax Assets for Unrealised Losses narrow-scope amendments.

These amendments have had no significant impact on the financial position of the Group.

The Group has not early adopted any standard, interpretation or amendment that has been issued but is not yet effective.

Comparatives

Comparative information has been amended where necessary to ensure consistency with the current period.

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 year ended 31 December 2017 is a period of twelve months from the date of approval of these financial statements ('the period of assessment').
In making this assessment, the Directors considered the Group's business, profitability projections, liquidity, funding and capital plans, under both base and plausible stress scenarios, together with a range of other factors such as the outlook for the UK economy. The Directors also considered the position of the Bank's parent, the Governor and Company of the Bank of Ireland as, in addition to being the Bank's sole shareholder, it is a provider of significant services to the Bank under outsourcing arrangements.

Going concern (continued)

The matters of primary consideration by the Directors are set out below:

Capital
The Group has developed capital plans in both base and stress scenarios and the Directors believe that the Group has sufficient capital to meet its regulatory capital requirements throughout the period of assessment.

Funding and liquidity
The Directors have considered the Group's funding and liquidity position and are satisfied that the Group has sufficient funding and liquidity throughout the period of assessment, including sufficient collateral for further funding if required from the Bank of England.

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

The Directors note that the Court 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 in respect of going concern.

Conclusion
On the basis of the above, the Directors 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 Group's ability to continue as a going concern over the period of assessment.

Group financial statements

(1) Subsidiaries
Subsidiary undertakings are investees (including structured entities) controlled by the Group. The Group controls an investee when it has power over the investee, is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The Group reassesses whether it controls an investee when facts and circumstances indicate that there are changes to one or more elements of control. The existence and effect of potential voting rights are considered when assessing whether the Group controls an investee only if the rights are substantive.

A structured entity is an entity designed so that its activities are not governed by way of voting rights. The Group assesses whether it has control over such entities by considering factors such as the purpose and design of the entity; the nature of its relationship with the entity; and the size of its exposure to the variability of returns from the entity.

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.

Business combinations
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 combinations involving entities or business 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 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. Foreign exchange gains and losses which arise on the retranslation to functional currency of intercompany monetary assets and liabilities are not eliminated.

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, over the entity's financial and operating decisions, generally accompanying a shareholding of between 20% and 50% of the voting rights.

A joint arrangement is an arrangement of which two or more parties have joint control.

A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Those parties are called joint venturers.

Investments in associates and joint ventures are accounted for by the equity method of accounting and are initially recognised at cost.

A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. Those parties are called joint operators.

The Group accounts for the assets, liabilities, revenues and expenses relating to its interest in joint

Group financial statements (continued)

operations in accordance with the IFRSs applicable to the particular assets, liabilities, revenues and expenses.

Accounting policies of associates and joint ventures 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. 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) 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 Sterling. 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 including mortgage discounts. Historical and forecast redemption data and management judgement of future performance are used to estimate the expected lives of mortgage and card assets and deposit liabilities.

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.

Interest income and expense (continued)

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

Operating profit includes the Group's earnings from ongoing activities after impairment charges and before share of profit or loss on joint ventures (after tax) and profit on disposal of business activities.

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 in 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.

A lease that does not transfer substantially all the risks and rewards of ownership are treated as operating leases. The annual rentals are credited to the income statement on a straight-line basis over the term of the lease. Costs incurred, including depreciation, are recognised in line with the normal depreciation policy for similar assets.

Lessee
The total payments made under operating leases are charged to the income statement on a straight line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Leases of property, plant and equipment where the Group has substantially all the risks and rewards of ownership, are classified as finance leases. Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included in long term payables. The interest element of the finance costs is charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

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.

(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. 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

Financial assets (continued)

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.

(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.

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.

The Group designates certain financial liabilities at fair value through profit or loss, as set out in note 34 to the consolidated financial statements and note x 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, DCF 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

Valuation of financial instruments (continued)

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.

Transfers between levels of the fair value hierarchy
The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change occurred. The Group provides these disclosures in note 35.

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.

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 highly probable future cash flows attributable to a recognised asset or liability, or a 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 (micro)
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. The hedged item in a micro fair value hedge is a single specified item e.g. a fixed commercial loan or an available for sale bond.

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 using the effective interest method.

(b) Fair value hedge (macro)
The hedged item in a macro fair value hedge is a pool of assets or liabilities with similar risk characteristics and profiles, such as a pool of fixed rate mortgages. Unlike micro fair value hedge accounting, macro fair value hedge accounting is not discontinued if an individual asset or liability within the pool of hedged items is sold, so long as the overall pool of hedged items retains its characteristics as documented at inception of the hedge. In addition, hedge effectiveness testing is performed on a portfolio basis rather than on an individual hedge relationship by hedge relationship basis.

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 using the effective interest method.

(c) 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.

Impairment of financial assets

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;
- (vii) initiation of bankruptcy proceedings; and
- (viii) granting a concession to a loan borrower for economic or legal reasons relating to the borrower's financial difficulty that would not be considered.

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.

When a loan is deemed uncollectible, it is derecognised and the provision for impairment is utilised. Subsequent recoveries 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 an agreed change ('forbearance measure') to a loan for reasons relating to the actual or apparent financial stress or distress of that borrower. Forbearance has not occurred 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.

Prior to any decision to grant forbearance the Group performs an assessment of a customer's financial circumstances and ability to repay. This assessment includes an individual assessment for impairment of the loan. 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 loans with similar credit risk characteristics and collectively assesses them for impairment.

Where the forborne loan 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.

Impairment of financial assets (continued)

Assets to which forbearance has been applied continue to be reported as forborne until such time as they satisfy conditions to exit forbearance in line with EBA guidance on non-performing and forborne classifications.

Where the cash flows from a forborne loan are considered to have expired, the original asset is derecognised and a new asset is recognised, initially measured at fair value. 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 loan is not directly linked to apparent financial stress or distress, these amendments are not considered forbearance. Any changes in expected cash flows are accounted for under IAS 39 i.e. the carrying amount of the asset is adjusted to reflect any change to 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 are 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.

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 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 and long leasehold 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.

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.
- Motor vehicles held for leasing - over the lease term.

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 directly 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 five 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.

(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.

(c) Goodwill
Goodwill represents 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. Goodwill on acquisition of subsidiaries is included in intangible assets.

Goodwill is tested annually for impairment or more frequently if there is any indication that it may be impaired, and carried at cost less accumulated impairment losses. Goodwill is allocated to cash generating units (CGU) for the purpose of impairment testing. An impairment loss arises if the carrying value of the CGU exceeds the recoverable amount. The recoverable amount of a CGU is the higher of its fair value less costs to sell and its value in use, where the value in use is the present value of the future cash flows expected to be derived from the CGU.

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 employees affected by the restructuring by starting to implement the plan or announcing its main features.

A levy payable to a Government is provided for on the occurrence of the event identified by the legislation that triggers the obligation to pay the levy.

Contingent liabilities are not recognised but are disclosed unless the probability of their occurrence is remote.

Employee benefits

(a) Pension obligations
The Group operates one defined benefit scheme, the NIIB Group Limited (1975) Pension Scheme. In addition, certain of the Group's employees are members of other Bank of Ireland Group schemes, and these are accounted for as defined contribution schemes in the Group. 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 and net interest on the net defined benefit liability / (asset) are recognised in profit or loss in operating expenses.

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.

Employee benefits (continued)

A settlement is a transaction that eliminates all further legal and constructive obligations for part or all of the benefits provided under a defined benefit plan, other than a payment of benefits to, or on behalf of, employees that is set out in the terms of the plan and included in the actuarial assumptions.

(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.

(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.

Income taxes

(a) Current income tax
Income tax payable on profits is recognised as an expense in the year in which profits arise. Tax provisions are provided on a transaction by transaction basis using a best estimate approach. 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.

A current tax provision is recognised when the Group has a present obligation as a result of a past event and it is probable that there will be a future outflow of funds to a fiscal authority to settle the obligation.

(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.

The tax effects of income tax losses available for carry forward are recognised as deferred tax assets 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 joint ventures, 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 recognised in 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. Income tax on items recognised directly in equity is recognised directly in equity.

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

a) Equity transaction costs
Incremental external costs directly attributable to equity transactions, including the issue of new equity stock or options, are shown as a deduction from equity, net of tax.

(b) 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.

(c) Available for sale reserve
The available for sale reserve represents the cumulative change in fair value of available for sale financial assets (net of tax and hedge accounting adjustments).

(d) Cash flow hedge reserve
The cash flow hedge reserve represents the cumulative changes in fair value (net of tax) 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.

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

(f) Capital redemption reserve fund
On 1 May 2015, preference stock of £300 million was repurchased. On the same date £300 million was transferred from capital contribution to the capital redemption reserve fund in order to identify these reserves as non-distributable.

(g) Other equity instruments
Other equity instruments represents Additional tier 1 securities issued by the Group to the Parent. See note 32 for details.

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is currently 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 in 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.

Financial guarantees

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 in provisions for undrawn contractually committed facilities and guarantees.

Operating segments

The Group's reportable operating 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.

Impact of new accounting standards not yet adopted

The following standards, interpretations and amendments to standards will be relevant to the Group but were not effective at 31 December 2017 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
IFRS 9, 'Financial instruments'

Nature of change
IFRS 9 'Financial instruments' has been endorsed by the EU as a replacement for IAS 39. It sets out requirements relating to recognition and derecognition, classification, measurement and hedge accounting. IFRS 9 retains but simplifies the mixed measurement model. Financial assets within its scope are required to be classified as being measured, subsequent to initial recognition, at amortised cost, fair value through other comprehensive income or fair value through profit or loss. The classification is dependent on both the overall objective of the business model within which the asset is held and the contractual cash flow characteristics of the asset. Impairment under IFRS 9 is forward-looking and is based on expected rather than incurred losses. For financial liabilities, there is no change to classification and measurement except for recognition of changes in own credit risk in other comprehensive income for certain liabilities designated at fair value through profit or loss. The Group is making the accounting policy choice allowed under IFRS 9 to continue to apply the hedge accounting requirements of IAS 39.

Effective date
Financial periods beginning on or after 1 January 2018.

Impact
The estimated quantitative impact on initial adoption of IFRS 9 is a reduction in stockholders' equity of approximately £40 million after tax, substantially all of which relates to an increase in the impairment loss allowance on loans and advances to customers.

Pronouncement
IFRS 15, 'Revenue from Contracts with Customers'

Nature of change
IFRS 15 specifies how and when revenue will be recognised as well as requiring entities to provide users of financial statements with more informative, relevant disclosures. The standard provides a single, principles based five-step model to be applied to all contracts with customers. The revised standard was endorsed by the EU on 22 September 2016.

Effective date
Financial periods beginning on or after 1 January 2018.

Impact
The Group has assessed the nature and extent of the impact of the standard which is not expected to be significant to the financial statements of the Group.

Pronouncement
IFRS 16 'Leases'

Nature of change
IFRS 16, 'Leases' addresses the definition of a lease, recognition and measurement of leases and establishes principles for reporting useful information to users of financial statements about the leasing activities of both lessees and lessors. A key change arising from IFRS 16 is that most operating leases will be accounted for on balance sheet for lessees. The accounting for lessors will not materially change. The standard replaces IAS 17 'Leases' and related interpretations. The revised standard was endorsed by the EU on 31 October 2017.

Effective date
Financial periods beginning on or after 1 January 2019 and earlier application is permitted if IFRS 15 'Revenue from contracts with customers' is applied at the same time.

Impact
The Group is currently assessing the nature and extent of the impact of the standard. The Group does not expect to early adopt the standard.

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, and this 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. This assessment is performed 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 significant management judgement 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 in each portfolio. In other circumstances, historical loss experience provides less relevant information about the incurred 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 51 to 53. See note 17 for an analysis of impairment provisions.

The estimation of impairment losses is subject to uncertainty 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.

(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 2017, the Group had a net deferred tax asset of £71 million (31 December 2016: £69 million), of which £74 million (31 December 2016: £76 million) related to trading losses. See note 23.

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

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 legislation includes a restriction of 25% on the amount of a bank's annual taxable profit that can be offset by pre-April 2015 carried forward losses. This restriction significantly lengthens the period over which the Group could use its UK trading losses and has been considered in the context of the measurement and recognition of the deferred tax asset at 31 December 2017.

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. It is currently projected that the deferred tax asset, in respect of tax losses will be recovered in full by the end of 2029.

Critical accounting estimates and judgements (continued)

(c) Unwind of fair value adjustments on acquired mortgages

Between 2012 and 2014 the Group acquired a number of tranches of mortgages from the Parent at fair value. These assets were 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 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. At 31 December 2017, the impact of the fair value adjustment was to reduce the carrying amount of loans and advances to customers by £251 million. (2016: £279 million). In 2017, there was a benefit of £28 million (2016: £50 million) to the income statement from the unwind of, and revisions to, the fair value adjustment.

There are two key judgements relating to the fair value adjustment. The first, and most significant, relates to the timing of the unwind of the fair value adjustment. This requires significant management judgement in relation to customer repayment assumptions which determines the expected lives of the relevant loans, and therefore impacts on the amount of interest income recognised in each financial year. In arriving at the expected lives and hence the amount of the unwind, a sensitivity analysis is carried out which considers the impact of various scenarios, as follows:

- lengthening the expected life on all mortgage portfolios by six months would give rise to an additional charge to the income statement of £21 million in 2017;
- shortening the expected life on all mortgage portfolios by six months would give rise to an additional credit to the income statement of £21 million in 2017; and
- retaining the attrition level on the Buy to Let portfolio at forecast 2017 levels for future years would give rise to an additional charge of £29 million to the income statement in 2017.

The second area of judgement relates to management's assessment of the level of future expected losses in the portfolio, with changes in expected losses being adjusted through net interest income over the expected life under the effective interest rate method.

(d) Impairment review of intangible assets

Impairment testing of intangible assets is an area involving significant management judgement, as it requires an assessment as to whether the carrying amount of the assets is appropriate when compared to its recoverable amount. The recoverable amount is estimated using projections based on the Group's most recent five year plans and applying a growth rate for subsequent years. These cash flows are then discounted at an appropriate discount rate.

The most critical assumptions underlying the impairment review are the cash flow projections in the Group's five year plan, as any reduction in these would reduce the recoverable amount. A significant reduction in these projections could lead to the relevant intangible asset being impaired.

At 31 December 2017 this exercise did not give rise to any impairment of intangible assets. As part of the impairment review process various sensitivity analyses are also carried out, considering both macroeconomic factors and Group specific variables, and the results of these supported the conclusion reached. Note 19 provides further information on the intangible assets and the associated assumptions.

(e) Effective interest rate

IAS 39 requires interest to be recognised using the effective interest rate, being the rate that exactly discounts estimated future cash flows over the expected life of the financial instrument to the net carrying amount of the financial instrument.

Adjustments to the carrying value of financial instruments may be required when actual cash flows vary from the initial estimation of future cash flows, with the corresponding adjustment being made to the income statement.

For secured mortgage lending management model future expected cash flows for each tranche of lending. In determining the future cash flows management use judgement to estimate the average life of each lending tranche. Management estimate expected payments of interest and capital based on expected interest rates and redemption profiles of customers based on previous customer behaviour, incorporating estimates of the proportion of borrowers expected to incur early redemption charges. Management considers the estimated life to be the most significant estimate, the accuracy of which could be impacted by customer behaviour being different to expectations. The impact of a one month decrease in expected life would be to reduce the value of loans on the balance sheet and interest income by c. £7.5 million in the year of change. During the year a charge of £12 million was recognised through interest income following a reassessment of the expected lives of loans and advances to customers.

For unsecured lending management model future expected cash flows for each tranche of credit card lending over the customer life which is currently estimated to be four years from origination. In determining the future cash flows management must use judgment to estimate customer behaviour including the card balance, transaction activity, repayment profiles and post-promotional retention rates based on previous customer experience and industry data. Management consider the most significant assumption to be linked to the level of future interest generating customer balances. A 10% reduction to the level of assumed future interest generating balances would be to reduce the value of loans on the balance sheet and interest income by c.£0.5 million in the year of change.

Notes to the Consolidated Financial Statements

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 retail products under the Bank of Ireland UK, Post Office, AA, Northridge, Marshall Leasing Limited and legacy Bristol & West brands. The Post Office product proposition includes deposits, mortgages, personal loans, current accounts, credit cards and travel cards, and foreign exchange services through the Group's joint venture operation under FRESH. The Group's investment in FRESH at 31 December 2017 was £61 million (2016: £61 million). The AA financial services proposition includes credit cards, loans, savings and mortgages.

Northern Ireland (NI)
The business includes the results of the Northern Ireland Bank of Ireland UK branch network and business centres, personal lending, 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 remains a managed deleverage of the loan book over the medium term.

Group Centre
This comprises the associated costs of management of the Group's funding, liquidity and capital position, together with the related costs of central risk and control functions along with employee costs and regulation costs including the 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. 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 84 to 98. The Group measures the performance of its operating segments through a measure of segmental profit or loss which is referred to as 'Underlying profit' 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.

Revenue
There were no revenues deriving from transactions with a single external customer that amounted to 10% or more of the Group's revenues.

2017	**GB Consumer Banking £m**	**NI £m**	**GB Business Banking £m**	**Group Centre £m**	**Total £m**
Net interest income	318	123	16	14	471
Other income / (expense)	(26)	24	3	(1)	-
Total operating income	**292**	**147**	**19**	**13**	**471**
Amortisation of intangible assets	(5)	-	-	-	(5)
Other operating expenses	(170)	(84)	(8)	(61)	(323)
Operating profit / (loss) before impairment charges on financial assets	**117**	**63**	**11**	**(48)**	**143**
Impairment (charges) / credit on financial assets	(17)	(10)	1	-	(26)
Share of profit after tax of joint venture	34	-	-	-	34
Underlying profit / (loss) before taxation	**134**	**53**	**12**	**(48)**	**151**
Profit on disposal of business activities	-	-	-	-	-
Profit / (loss) before tax	**134**	**53**	**12**	**(48)**	**151**

2016	GB Consumer Banking £m	NI £m	GB Business Banking £m	Group Centre £m	Total £m
Net interest income	338	126	18	15	497
Other income / (expense)	(27)	27	3	(6)	(3)
Total operating income	311	153	21	9	494
Amortisation of intangible assets	(6)	-	-	-	(6)
Other operating expenses	(168)	(83)	(10)	(46)	(307)
Operating profit / (loss) before impairment charges on financial assets	137	70	11	(37)	181
Impairment (charges) / credit on financial assets	(7)	(20)	4	-	(23)
Share of profit after tax of joint venture	35	-	-	-	35
Underlying profit / (loss) before taxation	165	50	15	(37)	193
Profit on disposal of business activities	-	-	-	-	-
Profit / (loss) before tax	165	50	15	(37)	193

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2 Interest income

Interest income	**2017 £m**	2016 £m
Loans and advances to customers	569	656
Finance leases and hire purchase receivables	58	55
Loans and advances to banks	24	38
Interest on hedging derivatives	(21)	(15)
Available for sale financial assets	15	16
Cash and balances with central banks	6	12
Interest income	**651**	**762**

Included in interest income for the year ended 31 December 2017 is £24 million in respect of income earned by the Group on loans and advances to banks, relating to amounts placed with the Parent (year ended 31 December 2016: £38 million) offset by interest on hedging derivatives of £21 million which are also held with the Parent (year ended 31 December 2016: £15 million).

Group share of joint operation interest income for the year ended 31 December 2017 is £16 million (year ended 31 December 2016: £6 million). Refer to note 18.

Also included in interest income for year ended 31 December 2017 is £9 million in respect of interest arising on financial assets, on which an impairment provision has been recognised (year ended 31 December 2016: £13 million). Interest income also includes £28 million relating to the unwind of, and revisions to, fair value adjustments associated with mortgages acquired from the Parent in prior years (year ended 31 December 2016: £50 million).

For the year ended 31 December 2017 interest recognised on total forborne loans and advances to customers was £10 million (year ended 31 December 2016: £18 million).

Finance lease and hire purchases receivables interest income arises from the Northridge business.

3 Interest expense

Interest expense	**2017 £m**	2016 £m
Customer accounts	137	216
Deposits from banks	19	25
Subordinated liabilities	24	24
Interest expense	**180**	**265**

Included in interest expense for the year ended 31 December 2017 is £36 million in respect of interest paid to the Parent on deposits and subordinated liabilities (year ended 31 December 2016: £49 million).

Group share of joint operation interest expense for the year ended 31 December 2017 is £7 million (year ended 31 December 2016: £4 million). Refer to note 18.

4 Fee and commission income and expense

Fee and commission income	**2017 £m**	2016 £m
ATM service fees	62	69
Banking fees and other commissions	30	27
Foreign exchange and credit card	20	20
Other	2	2
Fee and commission income	**114**	**118**
Amounts include:		
Group share of joint operation (note 18)	2	1

Fee and commission expense	**2017 £m**	2016 £m
Fee and commission expense - external	107	114
Fees paid to the Parent	8	7
Fee and commission expense	**115**	**121**
Amounts include:		
Group share of joint operation (note 18)	2	1

5 Net trading expense

Net trading expense	2017 £m	2016 £m
Financial assets designated at fair value through profit or loss	-	(2)
Financial liabilities designated at fair value through profit or loss	-	2
Other financial instruments held for trading	1	6
Net trading expense	**1**	**6**
Amounts include:		
Net trading (income) / expense from the Parent	(9)	18

Financial assets designated at fair value through profit or loss relate to certain 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 certain customer accounts, which are accounted for as financial liabilities designated at fair value through profit or loss.

Net trading expense from the Parent primarily comprises fair value movements on derivatives with the Parent which are in fair value hedge relationships.

6 Other operating income

	2017 £m	2016 £m
Other operating income	2	6

7 Operating expenses

Operating expenses	2017 £m	2016 £m
Administrative expenses		
Staff costs[1] (a)		
- Wages and salaries	39	29
- Social security costs	5	4
- Other pension costs[2]	10	6
Total staff costs	**54**	**39**
- Other administrative expenses (b)	49	42
- Other administrative expenses – related parties (c)	220	226
Amortisation on intangible assets (note 19)	5	6
Total operating expenses	**328**	**313**
Amounts include:		
Group share of joint operation (note 18)	21	12

(a) Staff costs
Staff costs of £54 million (year ended 31 December 2016: £39 million) include all gross salaries, related social security costs, and pension contributions attributable to those employees directly employed by the Group. Gross salaries also include those costs associated with staff seconded to the Group from the Parent under a secondment agreement. The monthly average number of staff (direct and seconded full time equivalents) was 715 (year ended 31 December 2016: 505), of which 594 related to the Bank (year ended 31 December 2016: 381). Refer to note 36 for details of compensation paid to key management personnel (KMP).

(b) Other administrative expenses
includes a net charge of £nil (year ended 31 December 2016: £4 million) in respect of the FSCS levy (see note 27).

(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 of 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 in 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.

[1] *Staff costs include amounts of £35 million (2016: £25 million) for wages and salaries, £5 million (2016: £4 million) for social security costs and £9 million (£5 million) for other pension costs recorded in the Bank financial statements.*
[2] *Other pension costs include £0.4 million (31 December 2016: £0.4 million) in relation to the NIIB scheme which is accounted for as a defined benefit scheme (see note 28) with the balance relating to other schemes which are accounted for on a defined contribution basis.*

8 Auditors' remuneration

	2017 £000's	2016 £000's
Fees payable for the audit of the Bank and Group financial statements	497	424
Audit of the Bank's subsidiaries pursuant to legislation	115	107
Audit related assurance services	9	9
Other assurance services	60	69
Auditors' remuneration	**681**	**609**

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 assurance 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

	2017 £m	2016 £m
Loans and advances to customers (note 17)	26	23
Impairment charges on financial assets	**26**	**23**

10 Share of profit after tax of joint venture

	2017 £m	2016 £m
First Rate Exchange Services Holdings Limited	34	35
Share of profit after tax of joint venture	**34**	**35**

This represents the Group's 50% share of profit after tax of its joint venture in FRESH with Post Office Limited. It is accounted for using the equity method of accounting. See note 18 for further information.

11 Taxation charge

	2017 £m	2016 £m
Current tax		
Current year charge	19	19
Total current taxation charge	**19**	**19**
Deferred tax		
Current year charge	3	5
Impact of corporation tax rate change	-	5
Adjustment in respect of prior year	(1)	-
Total deferred taxation charge	**2**	**10**
Taxation charge	**21**	**29**

The effective tax rate for the year is a charge of 14% (year ended 31 December 2016: charge of 15%). This rate is lower than the standard rate of 19.25% largely due to the impact of the treatment of the acquired mortgage portfolio and the impact of the results of the joint venture FRESH partly offset by the impact of the UK banking surcharge.

	2017 £m	2016 £m
Profit before taxation	**151**	**193**
Multiplied by the standard rate of Corporation tax in UK of 19.25% (2016: 20%)	29	39
Effects of:		
Non-allowable expenses	1	1
Share of results of joint venture after tax in the income statement	(7)	(7)
Impact of UK banking surcharge	4	3
Impact of corporation tax rate charge	-	5
Non-taxable income on the unwind of fair value adjustments on acquired mortgages (see page 98)	(5)	(11)
Other	(1)	(1)
Taxation charge	**21**	**29**

The reconciliation of tax on the profit before taxation, at the standard UK corporation tax rate, to the Group's actual tax charge for the years ended 31 December 2017 and 31 December 2016.

12 Cash and cash equivalents

Cash and cash equivalents	2017 £m	2016 £m
Cash	30	31
Balances at central banks	1,806	1,141
Total cash balances included in cash and cash equivalents	**1,836**	**1,172**
Loans and advances to banks	2,764	3,369
Less: amounts with a maturity of three months or more	(960)	(1,542)
Total loans and advances to banks included in cash and cash equivalents	**1,804**	**1,827**
Total cash and cash equivalents	**3,640**	**2,999**
Due from the Parent	434	495

13 Derivative financial instruments

	2017			2016		
	Contract notional amounts £m	Fair values Assets £m	Fair values Liabilities £m	Contract notional amounts £m	Fair values Assets £m	Fair values Liabilities £m
Derivatives held for trading						
Foreign exchange derivatives						
Currency forwards	156	3	1	176	3	8
Currency forwards – with the Parent	156	1	3	176	8	3
Currency swaps	207	4	1	166	2	5
Currency swaps - with the Parent	207	1	4	167	5	2
Total foreign exchange derivatives held for trading	**726**	**9**	**9**	**685**	**18**	**18**
Interest rate derivatives						
Interest rate swaps - with the Parent	2,064	3	2	1,677	5	2
Cross currency interest rate swaps - with the Parent	104	-	-	117	-	-
Total interest rate derivatives held for trading	**2,168**	**3**	**2**	**1,794**	**5**	**2**
Total derivatives held for trading	**2,894**	**12**	**11**	**2,479**	**23**	**20**
Derivatives held as fair value hedges						
Interest rate swaps - with the Parent	4,061	9	41	5,023	6	75
Derivatives held as cash flow hedges						
Interest rate swaps - with the Parent	3,590	6	13	2,950	26	7
Total derivative assets / liabilities held for hedging	**7,651**	**15**	**54**	**7,973**	**32**	**82**
Total derivative assets / liabilities	**10,545**	**27**	**65**	**10,452**	**55**	**102**

The Group's utilisation of objectives and policies in relation to managing the risks that arise in connection with derivatives, are included in the Risk Management section, on pages 59 to 60. 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.

During the year, the Group continued the process of moving from a gross flow cash hedging model to a derivatives hedging model, principally for interest rate risk management. As a result, £0.6 billion of balances owed to the Parent and £0.6 billion of balances owed from the Parent were repaid during 2017. In their place, the Group entered into new derivative transactions with the Parent. The Group has applied hedge accounting to the majority of these derivatives, which are classified as held for hedging in the table below.

The Group also holds certain derivatives to which hedge accounting is not applied and these are considered to be held for trading in the table below. These primarily include foreign exchange forward contracts with customers, with a corresponding foreign exchange contract to hedge foreign exchange risk with the Parent.

As set out in the risk management policy on page 38, the Group uses netting arrangements and collateral agreements to reduce its exposure to credit losses. Of the derivative assets of £27 million at 31 December 2017 (31 December 2016: £55 million):

- £20 million (31 December 2016: £50 million) are available for offset against derivative liabilities under CSA and ISDA standard documentation. These transactions do not meet the criteria under IAS 32 to enable the assets to be presented net of the liabilities. At 31 December 2017 cash collateral of £40 million (31 December 2016: £37 million) was placed against these liabilities and is reported in Loans and advances to banks (note 14); and
- £7 million (31 December 2016: £5 million) are not covered under CSA and ISDA standard documentation.

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 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:

2017	**Up to 1 year £m**	**1-2 years £m**	**2-5 years £m**	**Over 5 years £m**	**Total £m**
Forecast receivable cash flows	5	8	34	16	63
Forecast payable cash flows	(11)	(14)	(4)	-	(29)

2016	Up to 1 year £m	1-2 years £m	2-5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	5	4	26	16	51
Forecast payable cash flows	(1)	(1)	(2)	-	(4)

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

2017	**Up to 1 year £m**	**1-2 years £m**	**2-5 years £m**	**Over 5 years £m**	**Total £m**
Forecast receivable cash flows	6	9	34	14	63
Forecast payable cash flows	(12)	(13)	(4)	-	(29)

2016	Up to 1 year £m	1-2 years £m	2-5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	5	5	27	14	51
Forecast payable cash flows	(1)	(1)	(2)	-	(4)

During the years ended 31 December 2017 and 31 December 2016, there were no forecast transactions to which the Group had applied hedge accounting which were no longer expected to occur.

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14 Loans and advances to banks

	2017 £m	2016 £m
Placements with other banks	1,541	2,191
Mandatory deposits with central banks	1,223	1,178
Loans and advances to banks	**2,764**	**3,369**
Amounts include:		
Due from the Parent	1,394	2,038

Represented in placements with other banks is:
- an amount of £1,394 million (31 December 2016: £2,038 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 £1,989 million (31 December 2016: £1,912 million) are also disclosed in note 24. From a counterparty credit risk perspective, while 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
- £1 million included in amounts due from the Parent, whose return is dependent on movements in various external indices (31 December 2016: £63 million). These loans are designated at fair value through profit or loss. Refer to note 35 for details on fair value.

During the year ended 31 December 2017 £0.6 billion of balances were repaid by the Parent. For further details see note 36.

Represented in mandatory deposits with central banks is:
- an amount of £1,189 million relating to collateral with the Bank of England in respect of notes in circulation (31 December 2016: £1,142 million). £683 million of this relates to non-interest bearing collateral (31 December 2016: £644 million); and
- an amount of £34 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 2016: £36 million).

15 Available for sale financial assets

	2017 £m	2016 £m
Government bonds	428	585
Debt securities listed	580	555
Available for sale financial assets	**1,008**	**1,140**

At 31 December 2017 and at 31 December 2016, no available for sale financial assets were pledged in sale and repurchase agreements.

Movements on available for sale financial assets	2017 £m	2016 £m
At 1 January	1,140	956
Revaluation adjustments	(12)	20
Additions	82	301
Redemptions / disposals	(198)	(133)
Amortisation	(4)	(4)
At 31 December	**1,008**	**1,140**

16 Loans and advances to customers

	2017 £m	2016 £m
Loans and advances to customers	18,741	18,860
Finance leases and hire purchase receivables (see below)	1,411	1,227
Gross loans and advances to customers	**20,152**	**20,087**
Less: allowance for impairment charges on loans and advances to customers (note 17)	(155)	(266)
Loans and advances to customers	**19,997**	**19,821**
Amounts include:		
Group share of joint operation (note 18)	360	184
Due from entities controlled by the Parent	6	6

Finance leases and hire purchase receivables

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

	2017 £m	2016 £m
Gross investment in finance leases:		
Not later than 1 year	491	449
Later than 1 year and not later than 5 years	1,027	876
Later than 5 years	5	4
	1,523	**1,329**
Unearned future finance income on finance leases	(112)	(102)
Net investment in finance leases	**1,411**	**1,227**
Not later than 1 year	455	415
Later than 1 year and not later than 5 years	951	808
Later than 5 years	5	4
	1,411	**1,227**

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

At 31 December 2017 the accumulated allowance for uncollectable minimum lease payments receivable was £nil (31 December 2016: £nil).

Refer to note 24 for further details.

Securitisations

At 31 December 2017 loans and advances to customers include £2,886 million (31 December 2016: £3,397 million) of residential mortgage balances that have been securitised but not derecognised. Refer to note 38. The assets, or interests in the assets, were transferred to a structured entity, 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.

17 Impairment provisions

2017	Residential mortgages £m	Non-property SME and corporate £m	Commercial property and construction £m	Consumer £m	Total impairment provisions £m
Provision at 1 January 2017	28	58	152	28	266
Exchange adjustments	-	1	1	-	2
Provisions utilised	(2)	(31)	(106)	(16)	(155)
Recoveries	(1)	2	5	5	11
Other movements	-	1	3	1	5
Charge to the income statement	2	1	8	15	26
Provision at 31 December 2017	**27**	**32**	**63**	**33**	**155**

17 Impairment provisions (continued)

2016	Residential mortgages £m	Non-property SME and corporate £m	Commercial property and construction £m	Consumer £m	Total impairment provisions £m
Provision at 1 January 2016	30	92	295	37	454
Transfer between provisions	-	-	-	-	-
Exchange adjustments	-	3	8	-	11
Provisions utilised	(3)	(40)	(176)	(19)	(238)
Recoveries	-	1	3	6	10
Other movements	(1)	2	5	-	6
Charge to the income statement	2	-	17	4	23
Provision at 31 December 2016	28	58	152	28	266

18 Interest in joint venture and joint operations

A joint arrangement is an arrangement of which two or more parties have joint control i.e. contractually agreed sharing of control of an arrangement where decisions about the relevant activities require the unanimous consent of the parties sharing control. These arrangements are identified by reference to the power sharing agreements, ensuring that unanimous consent of all parties is a requirement. Where the arrangement has been structured through a separate vehicle, the Group has accounted for it as a joint venture. Where no separate vehicle exists, the arrangements are accounted for as a joint operation.

Joint arrangement	**Holding**	**Classification**	**Country of operation**	**Nature of activities**
First Rate Exchange Services Holdings Limited	50%	Joint venture	UK	Sale of foreign exchange products through the UK Post Office network
AA Financial Services	n/a	Joint operation	UK	Sale of AA branded credit cards, unsecured personal loans, savings and mortgages

Joint venture

The Group owns 50% of the shares in FRESH, a company incorporated in the United Kingdom which provides foreign exchange services.

The following table shows the movement in the Group's interest in FRESH during the year ended 31 December 2017 and 31 December 2016.

The investment in FRESH is unquoted and is measured using the equity method of accounting. There are no significant restrictions on the ability of this entity to transfer funds to the Group in the form of cash dividends, or to repay loans or advances made by the Group, nor is there any unrecognised share of losses either for the year ended 31 December 2017 or cumulatively in respect of this entity. The Group does not have any further commitments or contingent liabilities in respect of this entity other than its investment to date.

There are no significant risks associated with the joint venture that have been identified which require disclosure.

	2017 £m	2016 £m
At 1 January	61	60
Share of profit after taxation (note 10)	34	35
Dividends received	(34)	(35)
Other	-	1
At 31 December	**61**	**61**

18 Interest in joint venture and joint operations (continued)

The following amounts represent the Group's 50% share of the revenue, expenses, assets and liabilities of FRESH for the year ended 31 December 2017 and the year ended 31 December 2016.

	2017 £m	2016 £m
Revenue	70	68
Expenses	(28)	(23)
Profit before taxation	**42**	**45**
Taxation charge	(8)	(10)
Profit after taxation	**34**	**35**
Non-current assets	9	6
Current assets	214	186
Total assets	**223**	**192**
Current liabilities	(162)	(131)
Total liabilities	**(162)**	**(131)**
Net assets	**61**	**61**

Joint operation – AA Financial Services
In July 2015, the Group entered into a strategic partnership with AA Financial Services for the sale of AA branded credit cards, unsecured personal loans, savings and mortgages.

The above joint arrangement has been accounted for as a joint operation, on the basis that it is not a separate legal entity.

The Group combines its share of the joint operation in individual income and expenses, assets and liabilities and cash flows on a line-by-line basis.

19 Intangible assets

	2017				2016			
	Goodwill £m	**Computer software internally generated £m**	**Other externally purchased intangible assets £m**	**Total £m**	Goodwill £m	Computer software internally generated £m	Other externally purchased intangible assets £m	Total £m
Cost								
At 1 January	-	35	76	111	-	34	76	110
Acquisitions (note 20)	35	-	5	40	-	-	-	-
Additions	-	-	1	1	-	1	-	1
At 31 December	**35**	**35**	**82**	**152**	**-**	**35**	**76**	**111**
Accumulated amortisation								
At 1 January	-	(34)	(52)	(86)	-	(34)	(46)	(80)
Charge to the income statement (note 7)	-	-	(5)	(5)	-	-	(6)	(6)
At 31 December	**-**	**(34)**	**(57)**	**(91)**	**-**	**(34)**	**(52)**	**(86)**
Net book value at 31 December	**35**	**1**	**25**	**61**	**-**	**1**	**24**	**25**

Goodwill of £35 million and intangible assets of £5 million arose on the acquisition of Marshall Leasing Limited on 24 November 2017, as set out in note 20. Goodwill is not amortised as it is deemed to have an indefinite useful life. The Group's investment in Marshall Leasing Limited has been reviewed for impairment for the purpose of December 2017 reporting and no impairment was identified as a result of this review.

Other Intangible assets have also been reviewed for any indication that impairment may have occurred. No impairment was identified in the year ended 31 December 2017 or 31 December 2016. 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 of these intangible assets, management notes that a possible break even scenario would be if the following assumptions were used:

- If the current forecast income was reduced by 15%; and
- If the current forecast costs increased by 12%.

20 Acquisition of Marshall Leasing Limited

	2017 Provisional £m
Fair value of consideration transferred	**42**
Recognised amounts of identifiable net assets:	
Property, plant and equipment	79
Intangible assets	5
Other assets	5
Deferred tax assets	2
Deposits from banks	(71)
Other liabilities	(12)
Current tax	(1)
Net identifiable assets and liabilities	**7**
Goodwill	**35**

On 24 November 2017 the Group acquired 100% of the ordinary share capital of Marshall Leasing Limited (MLL), a car and commercial vehicle leasing and fleet management company based in Cambridge, UK. This acquisition will help Northridge Finance to continue to develop and diversify its business.

The acquisition was settled in cash of £42 million to purchase 100% of the ordinary share capital of Marshall Leasing Limited.

Due to the proximity of the acquistion to the balance sheet date, the difference between the book value of acquired net assets and consideration payable has been provisionally recognised as goodwill and intangible assets. During 2018, the Group will determine the fair value of identifiable net assets acquired and liabilities and contingent liabilities assumed, with any corresponding adjustment necessary being made to the value of goodwill and intangible assets recognised.

Acquisition-related costs amounting to £1 million have been recognised as an expense in the consolidated income statement, as part of operating expenses.

Goodwill recognised on the acquisition date relates to the expected growth, cost synergies and the value of MLL's workforce which cannot be separately recognised as an intangible asset. This goodwill has been allocated to the Group's GB Consumer Banking segment and is not expected to be deductible for tax purposes.

The acquisition of MLL has had no material impact on the Group's total operating income and operating profit respectively, from the acquisition date to 31 December 2017. For the full year ended 31 December 2017, MLL had total revenue of £21 million (net of depreciation on rental vehicles of £19 million) and operating profit of £4 million.

21 Property, plant and equipment

	2017				2016			
	Computer and other equipment £m	**Freehold land and builldings and long leaseholds (held at fair value) £m**	**Vehicles leased under operating leases £m**	**Total £m**	Computer and other equipment £m	Freehold land and builldings and long leaseholds (held at fair value) £m	Vehicles leased under operating leases £m	Total £m
Cost or valuation								
At 1 January	1	7	-	8	1	7	-	8
Acquisition of subsidiary undertakings (note 20)	-	-	79	79	-	-	-	-
Revaluation adjustments	-	1	-	1	-	-	-	-
Additions	-	15	4	19	-	-	-	-
Disposals / write offs	-	-	(1)	(1)	-	-	-	-
At 31 December	**1**	**23**	**82**	**106**	**1**	**7**	**-**	**8**
Accumulated depreciation								
At 1 January	-	-	-	-	-	-	-	-
Charge for the year	-	-	2	2	-	-	-	-
At 31 December	**-**	**-**	**2**	**2**	**-**	**-**	**-**	**-**
Net book value at 31 December	**1**	**23**	**80**	**104**	**1**	**7**	**-**	**8**

The historical cost of property, plant and equipment held at fair value at 31 December 2017 was £22 million (31 December 2016: £7 million). No depreciation is charged on freehold land and buildings and long leaseholds, as these are revalued annually.

21 Property, plant and equipment (continued)

Future capital expenditure
The table below shows future capital expenditure in relation to both property, plant and equipment and intangible assets.

Future capital expenditure	2017 £m	2016 £m
Authorised by the Directors but not contracted	-	15

The Group has commitments on future rentals under non-cancellable operating leases as follows:

Operating leases	Payable 2017 £m	Payable 2016 £m
Not later than 1 year	4	1
Later than 1 year and not later than 5 years	14	4
Later than 5 years	20	16
	38	**21**

The Group has the following amounts of minimum lease receivables under non-cancellable operating leases as follows:

Operating lease receivables	Receivable 2017 £m	Receivable 2016 £m
Not later than 1 year	21	-
Later than 1 year and not later than 5 years	25	-
Later than 5 years	1	-
	47	**-**

22 Other assets

Other assets	2017 £m	2016 £m
Sundry and other receivables	54	51
Accounts receivable and prepayments	34	37
Interest receivable	18	21
Other assets	**106**	**109**
Amounts include:		
Due from the Parent	1	3
Maturity profile of other assets		
Amounts receivable within 1 year	89	88
Amounts receivable after 1 year	17	21

23 Deferred tax

	2017 £m	2016 £m
The movement on the deferred tax account is as follows:		
At 1 January	69	86
Income statement charge for the year (note 11)	(2)	(10)
Available for sale securities - charge to other comprehensive income	-	(1)
Cash flow hedges - credit / (charge) to other comprehensive income	3	(7)
Additional tier 1 - credit to equity	1	2
Other movements	-	(1)
At 31 December	**71**	**69**
Deferred tax assets and liabilities are attributable to the following items:		
Deferred tax assets		
Unutilised tax losses	74	76
Fixed / leased assets	8	6
Other	-	1
Total deferred tax assets	**82**	**83**
Deferred tax liabilities		
Cash flow hedges	(8)	(11)
Available for sale securities	(1)	(2)
Deferred tax on property held at fair value	(1)	(1)
Other	(1)	-
Total deferred tax liabilities	**(11)**	**(14)**
Represented on the balance sheet as follows:		
Deferred tax assets	71	69
Total deferred tax	**71**	**69**

In accordance with IAS 12, in presenting the deferred tax balances above the Group offsets deferred tax assets and liabilities where:

- an entity has a legally enforceable right to set off current tax assets against current tax liabilities; and
- the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority on the same taxable entity.

The UK corporation tax rate reduced to 19% for the years beginning on or after 1 April 2017 and will reduce to 17% for years beginning on or after 1 April 2020.

24 Deposits from banks

	2017 £m	2016 £m
Deposits from banks	**3,561**	2,691
Amounts include:		
Due to the Parent	1,989	1,912

Deposits from banks includes £1,200 million (31 December 2016: £600 million) of borrowings under the Bank of England Term Funding Scheme, which is collateralised with mortgage loans, and £350 million (31 December 2016: £155 million) borrowed under the Bank of England Indexed Long - Term Repo scheme, which is collateralised with notes issued by Bowbell (see note 38). Drawings under the Term Funding Scheme will be repaid within four years from the date of drawdown. The interest to be charged is based on the quantum of net lending by the Bank and by the Parent's UK branch to UK resident households, private non-financial corporations and certain non-bank credit providers from June 2016 to December 2017.

Amounts due to the Parent of £1,989 million (31 December 2016: £1,912 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 36 in respect of changes in these balances during 2017.

25 Customer accounts

	2017 £m	2016 £m
Term deposits	6,492	8,774
Demand deposits	9,622	8,145
Non-interest bearing current accounts	2,492	2,188
Interest bearing current accounts	355	368
Customer accounts	**18,961**	**19,475**
Amounts include:		
Group share of joint operation (note 18)	297	212
Due to entities controlled by the Parent	8	7

Term deposits include deposits of £1 million (31 December 2016: £63 million), whose return is dependent on movements in various external indices, and these deposits are designated at fair value through profit or loss. Refer to note 35 for details on fair value.

26 Other liabilities

	2017 £m	2016 £m
Notes in circulation	1,084	1,036
Accrued interest payable	52	78
Sundry payables	82	73
Accruals and deferred income	15	13
Other liabilities	**1,233**	**1,200**
Amounts include:		
Due to the Parent	2	8
Group share of joint operation (note 18)	7	5
Maturity profile of other liabilities		
Amounts payable within 1 year	1,233	1,199
Amounts payable after 1 year	-	1

The Bank is authorised to issue banknotes in Northern Ireland under the Bank of Ireland (UK) plc Act 2012.

27 Provisions

31 December 2017	**FSCS £m**	**Other £m**	**Total £m**
At 1 January	5	11	16
Net charge to the income statement	-	11	11
Utilised during the year	(3)	(11)	(14)
At 31 December	**2**	**11**	**13**
Expected utilisation period			
Used within 1 year	2	9	11
Used after 1 year	-	2	2

Financial services compensation scheme
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 financial 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 ongoing 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 provision at 31 December 2017 represents the Group's estimate of the interest element of the levy due for the FSCS levy year from 1 April 2017 to 31 March 2018. This is calculated based on the Group's share of industry protected deposits at 31 December 2016.

The charge to the income statement for 2017 of £2 million has been offset by a write back of opening provision of £2 million.

Other
As at 31 December 2017 a provision of £6 million has been made for certain commissions payable to the Post Office. In addition, as at 31 December 2017 the Group has a provision of £5 million to cover potential payments to customers in relation to various compliance matters. The provision is based upon management's current expectations of future payments to be made to customers.

28 Retirement benefit obligations

The Group's employees' 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 future service contribution to those particular schemes. The Group does not have any liability for payment in respect of increases 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. Consequently, the schemes have been accounted for as defined contribution schemes in these financial statements and where applicable will be included in the disclosures for defined benefit schemes in the financial statements of BoI Group.

NIIB Group Limited (1975) Pension Scheme (the 'NIIB scheme')
The NIIB defined benefit scheme is based on final pensionable salary and operates for eligible employees of NIIB Group Limited and its subsidiaries. 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, Willis Towers Watson.

The scheme has been closed to new members since late 2006.

Regulatory framework
The NIIB scheme operates under the UK pension 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 the 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) and discounted based on the return expected from assets held in accordance with the actual scheme investment policy.

The trustees' other duties include managing the investment of the plan assets, administration of the plan benefits, ensuring contributions are received, compliance with relevant legislation and exercising of discretionary powers. The Group works closely with the trustees, who manage the plan.

Actuarial valuation of the NIIB scheme
A formal valuation of the NIIB scheme was carried out as at 1 May 2016. 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 were completed in 2017 and a schedule of contributions and recovery plan, setting out how the shortfall in the scheme will be met, was agreed between the trustees and the Group and submitted to, and signed off by, the Pensions Regulator.

Under the schedule of contributions the Group agreed to make contributions of £1.31 million by 1 August 2017 plus £1.095 million by 1 April 2018, to meet the shortfall in the scheme of £3.0 million as at the date of the triennial valuation, in addition to the cost of future benefit accrual. The next formal valuation of the NIIB scheme is due to be carried out as at 1 May 2019.

Plan details
The following table sets out details of the membership of the NIIB scheme as at 1 May 2016.

Plan details at last valuation date	By number	By % of scheme liability
Scheme members		
Active	70	30
Deferred	122	28
Pensioners / dependants	68	42

28 Retirement benefit obligations (continued)

Financial and demographic assumptions
The assumptions used in calculating the costs and obligations of the NIIB scheme, as detailed below, were set after consultation with Willis Towers Watson.

The discount rate used to determine the present value of the obligations is set by reference to market yields on corporate bonds. The methodology was updated at the end of 2017, primarily to remove a number of bonds that did not obviously meet the criteria of 'corporate bonds' from the universe considered.
The methodology used to determine the assumption for retail price inflation was updated at the end of 2017. It now uses an inflation curve derived by Willis Towers Watson using market data which reflects the characteristics of the Bank's liabilities with an appropriate adjustment to reflect distortions due to supply and demand.
The assumption for consumer price inflation is set by reference to retail price inflation, with an adjustment applied, as no consumer price inflation linked bonds exist.

The salary assumption takes into account inflation, seniority, promotion and current employment market relevant to the Group.

Financial assumptions
The financial assumptions used in measuring the Group's defined benefit liability under IAS 19 are set out in the table below.

Financial assumptions	**2017 % p.a.**	2016 % p.a.
Consumer price inflation	2.20	2.40
Retail price inflation	3.20	3.40
Discount rate	2.75	2.55
Rate of general increase in salaries	3.70	3.90
Rate of increase in pensions in payment	3.00	3.00
Rate of increase in deferred pensions	2.20	2.40

Mortality assumptions
The mortality assumptions adopted are outlined in the table below.

Post retirement mortality assumptions	**2017 Years**	2016 Years
Longevity at age 70 for current pensioners		
Men	18.5	18.5
Women	19.9	20.0
Longevity at age 60 for active members currently aged 60 years		
Men	27.7	28.0
Women	29.4	29.8
Longevity at age 60 for active members currently aged 40 years		
Men	29.3	29.8
Women	30.9	31.7

Amounts recognised in financial statements
The table below outlines where the Group's defined benefit plans are recognised in the financial statements.

	2017 £m	2016 £m
Total charge in operating expenses	**(1)**	**-**
Total gain in remeasurements[1]	**7**	**(4)**
Total asset in the balance sheet	**8**	**-**

[1] *Shown before deferred tax.*

28 Retirement benefit obligations (continued)

The movement in the net defined benefit obligation is as follows:

	2017			2016		
	Present value of obligation £m	**Fair value of plan assets £m**	**Surplus / (deficit) of plan £m**	Present value of obligation £m	Fair value of plan assets £m	Surplus / (deficit) of plan £m
At 1 January	**(40)**	**40**	**-**	**(30)**	**32**	**2**
Current service cost	(1)	-	(1)	-	-	-
Interest (expense) / income	(1)	1	-	(1)	1	-
Total amount in recognised income statement	**(2)**	**1**	**(1)**	**(1)**	**1**	**-**
Return on plan assets not included in income statement	-	3	3	-	6	6
Change in demographic assumptions	1	-	1	1	-	1
Change in financial assumptions	3	-	3	(10)	-	(10)
Experience losses	-	-	-	(1)	-	(1)
Total remeasurements in other comprehensive income	**4**	**3**	**7**	**(10)**	**6**	**(4)**
Benefit payments	1	(1)	-	1	(1)	-
Employer contributions	-	2	2	-	2	2
Other	(1)	1				
Other movements	**-**	**2**	**2**	**1**	**1**	**2**
At 31 December	**(38)**	**46**	**8**	**(40)**	**40**	**-**

Asset breakdown	**2017 £m**	2016 £m
Equities (quoted)	28	24
Index linked government bonds (quoted)	18	16
Total fair value of assets	**46**	**40**

Sensitivity of defined benefit obligation to key assumptions
The table sets out how the defined benefit obligation would have been affected by changes in the significant actuarial assumptions that were reasonably possible at 31 December 2017.

Some of the 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 a 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. The methods and types of assumptions used in preparing the sensitivity analysis are unchanged compared to the prior year.

Impact on defined benefit obligation	**Change in assumptions**	**Increase in assumptions £m**	**Decrease in assumptions £m**
Discount rate	0.25%	(2.0)	2.2
Inflation[1]	0.1%	0.5	(0.5)
Salary growth	0.1%	0.2	(0.2)
Life expectancy	1 year	1.1	(1.1)

[1] *Including other inflation-linked assumptions (consumer price inflation, pension increases, salary growth).*

28 Retirement benefit obligations (continued)

Years	Benefit payments from plan assets £m
2018 - 2027	(11)
2028 - 2037	(18)
2038 - 2047	(25)
2048 - 2057	(27)
2058 - 2067	(21)
2068 - 2077	(12)
2078 - 2087	(4)
2088 - 2097	(1)
	(119)

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 2018 are £1.7 million. Expected employee contributions for the year ended 31 December 2018 are £53,000.

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 addresses only 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	A significant proportion 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.

29 Subordinated liabilities

	2017 £m	2016 £m
£90 million subordinated floating rate loans 2022[1]	-	90
£45 million subordinated floating rate loans 2022[2]	-	45
£200 million subordinated floating rate notes 2025[3]	200	200
£90 million subordinated floating rate notes 2027[4]	90	-
Subordinated liabilities	**290**	**335**

Movement on subordinated liabilities	2017 £m	2016 £m
At 1 January	335	335
Issued during the year	90	-
Repurchased	(135)	-
At 31 December	**290**	**335**

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.

30 Contingent liabilities and commitments

	2017 £m	2016 £m
Contingent liabilities		
Guarantees and irrevocable letters of credit	9	9
Other contingent liabilities	5	5
Total contingent liabilities	**14**	**14**
Commitments		
Undrawn formal standby facilities, credit lines and other commitments to lend		
- revocable or irrevocable with original maturity of 1 year or less	4,224	3,501
- irrevocable with original maturity of over 1 year	47	173
Total commitments	**4,271**	**3,674**

The table sets out 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.

Guarantees and letters of credit are given as security to support the performance of a customer to third parties. As the Group will be required to meet these obligations only 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. Other contingent liabilities also include documentary credits which 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.

[1] *Initial call date 18 July 2017. This was rolled forward at its initial call date and was redeemed on 19 December 2017.*
[2] *Redeemed on initial call date on 19 December 2017.*
[3] *Inital call date 26 November 2020. If not repaid at this point, they are due in full on their final maturity date of 26 November 2025. They bear interest at a floating rate of 4.225% per annum above the sterling LIBOR three month rate.*
[4] *Initial call date 19 December 2022. If not repaid at this point, they are due in full on their maturity date of 19 December 2027. They bear interest at a floating rate of 2.72% per annum above the sterling LIBOR three month rate.*

31 Share capital

	Ordinary Shares[1]	
	2017 £m	2016 £m
At 1 January and 31 December	851	851

At 31 December 2017 and at 31 December 2016, all shares issued by the Group were held by the Parent and were fully paid.

32 Other equity instruments

	2017 £m	2016 £m
At 1 January and 31 December	300	300

Other equity instruments consist of Additional tier 1 securities held by the Parent:

- £200 million issued on 1 May 2015; and
- £100 million issued on 26 November 2015

The principal terms of the Additional tier 1 securities are as follows:

- the securities constitute direct, unsecured and subordinated obligations of the Group, rank behind Tier 2 instruments and in priority to ordinary shareholders;
- the securities bear a fixed rate of interest (7.875% for the May 2015 issuance; 8.4% for the November 2015 issuance) until the first call date (1 May 2020 and 26 November 2020 respectively). After the initial call date, in the event that they are not redeemed, the Additional tier 1 securities will bear interest at rates fixed periodically in advance for five-year periods based on market rates at that time;
- the Group may elect at its sole and full discretion to cancel (in whole or in part) the interest otherwise scheduled to be paid on any interest payment date;
- the securities have no fixed redemption date, and the security holders will have no right to require the Group to redeem or purchase the securities at any time;
- the Group may, in its sole and full discretion, but subject to the satisfaction of certain conditions, elect to redeem all (but not some only) of the securities on the initial call date or on any interest payment date thereafter. In addition, the Additional tier 1 securities are repayable, at the option of the Group, due to certain regulatory or tax reasons. Any repayments require the prior consent of the regulatory authorities; and
- the securities will convert into ordinary shares if the Group's CET 1 ratio (on a CRD IV full implementation basis) falls below 7%.

[1] *All shares issued are in denominations of £1, therefore the table above also represents unit values.*

33 Liquidity risk

The tables below summarise the maturity profile of the Group's financial liabilities, at 31 December 2017 and at 31 December 2016, based on contractual undiscounted repayment obligations. See also Risk Management section 2.2 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 shown below 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 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 as 'demand'.

2017 **Maturity profile of financial liabilities**	**Demand** **£m**	**0-3 months** **£m**	**3-12 months** **£m**	**1-5 years** **£m**	**Over 5 years** **£m**	**Total** **£m**
Deposits from banks	315	155	1,242	1,865	45	3,622
Customer accounts	14,039	2,043	2,424	545	-	19,051
Subordinated liabilities	-	3	9	53	339	404
Contingent liabilities	14	-	-	-	-	14
Commitments	3,218	20	987	46	-	4,271
Total	**17,586**	**2,221**	**4,662**	**2,509**	**384**	**27,362**

2016 Maturity profile of financial liabilities	Demand £m	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Deposits from banks	349	162	439	1,737	58	2,745
Customer accounts	12,938	2,613	3,210	846	2	19,609
Subordinated liabilities	-	7	16	98	391	512
Contingent liabilities	14	-	-	-	-	14
Commitments	3,056	19	426	173	-	3,674
Total	16,357	2,801	4,091	2,854	451	26,554

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.

2017 **Maturity profile of derivative liabilities**	**Demand** **£m**	**0-3 months** **£m**	**3-12 months** **£m**	**1-5 years** **£m**	**Over 5 years** **£m**	**Total** **£m**
Gross settled derivative liabilities - outflows	(11)	(210)	(197)	(16)	-	(434)
Gross settled derivative liabilities - inflows	11	205	193	16	-	425
Gross settled derivative liabilities - net flows	-	(5)	(4)	-	-	(9)
Net settled derivative liabilities	-	(7)	(11)	(31)	(4)	(53)
Total derivatives cash flows	**-**	**(12)**	**(15)**	**(31)**	**(4)**	**(62)**

2016 Maturity profile of derivative liabilities	Demand £m	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Gross settled derivative liabilities - outflows	(20)	(203)	(141)	(11)	-	(375)
Gross settled derivative liabilities - inflows	20	192	134	11	-	357
Gross settled derivative liabilities - net flows	-	(11)	(7)	-	-	(18)
Net settled derivative liabilities	-	(10)	(19)	(48)	(5)	(82)
Total derivatives cash flows	-	(21)	(26)	(48)	(5)	(100)

34 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.

2017	**At fair value through profit or loss**			**At fair value through Other Comprehensive income (OCI)**			
	Derivatives designated as fair value hedging instruments £m	**Held for trading £m**	**Designated upon initial recognition £m**	**Available for sale £m**	**Cash flow hedge derivatives £m**	**Held at amortised cost £m**	**Total £m**
Financial assets							
Cash and balances with central banks	-	-	-	-	-	1,836	1,836
Items in the course of collection from other banks	-	-	-	-	-	192	192
Derivative financial instruments	9	12	-	-	6	-	27
Loans and advances to banks	-	-	1	-	-	2,763	2,764
Available for sale financial assets	-	-	-	1,008	-	-	1,008
Loans and advances to customers	-	-	-	-	-	19,997	19,997
Total financial assets	**9**	**12**	**1**	**1,008**	**6**	**24,788**	**25,824**
Financial liabilities							
Deposits from banks	-	-	-	-	-	3,561	3,561
Customer accounts	-	-	1	-	-	18,960	18,961
Items in the course of transmission to other banks	-	-	-	-	-	108	108
Derivative financial instruments	41	11	-	-	13	-	65
Subordinated liabilities	-	-	-	-	-	290	290
Total financial liabilities	**41**	**11**	**1**	**-**	**13**	**22,919**	**22,985**

2016	At fair value through profit or loss			At fair value through Other Comprehensive income (OCI)			
	Derivatives designated as fair value hedging instruments £m	Held for trading £m	Designated upon initial recognition £m	Available for sale £m	Cash flow hedge derivatives £m	Held at amortised cost £m	Total £m
Financial assets							
Cash and balances with central banks	-	-	-	-	-	1,172	1,172
Items in the course of collection from other banks	-	-	-	-	-	131	131
Derivative financial instruments	6	23	-	-	26	-	55
Loans and advances to banks	-	-	63	-	-	3,306	3,369
Available for sale financial assets	-	-	-	1,140	-	-	1,140
Loans and advances to customers	-	-	-	-	-	19,821	19,821
Total financial assets	6	23	63	1,140	26	24,430	25,688
Financial liabilities							
Deposits from banks	-	-	-	-	-	2,691	2,691
Customer accounts	-	-	63	-	-	19,412	19,475
Items in the course of transmission to other banks	-	-	-	-	-	85	85
Derivative financial instruments	75	20	-	-	7	-	102
Subordinated liabilities	-	-	-	-	-	335	335
Short positions in trading securities	-	-	-	-	-	-	-
Total financial liabilities	75	20	63	-	7	22,523	22,688

34 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.

	2017		2016	
	Fair values £m	**Contractual amount due on maturity £m**	Fair values £m	Contractual amount due on maturity £m
Customer accounts	1	1	63	59

35 Fair value of assets and liabilities

Fair value of assets and liabilities
Fair value 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 DCF 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 recognised and subsequently measured at fair value
All financial instruments are initially recognised at fair value. The Group subsequently measures derivatives, available for sale financial assets and certain other financial assets and liabilities designated at fair value through profit or loss at fair value in the balance sheet. These instruments are shown as at fair value through profit or loss or at fair value through other comprehensive income in note 34 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 DCF 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 held at amortised cost
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.

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).

35 Fair value of assets and liabilities

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 of non-financial assets

Property
A revaluation of Group property was carried out as at 31 December 2017. All freehold and long leasehold commercial properties were valued by Lisney (or its partner, Sanderson Weaterall) as external valuers. Lisney valuations were made on the basis of observable inputs such as comparable lettings and sales (level 2 inputs). Unobservable inputs such as profile, lot size, layout and presentation of accommodation are also used (level 3 inputs). Using reasonably possible alternative assumptions would not have a material impact on the value of these assets. All properties are valued based on highest and best use.

35 Fair value of assets and liabilities (continued)

	2017 Level 1 £m	2017 Level 2 £m	2017 Level 3 £m	2017 Total £m	2016 Level 1 £m	2016 Level 2 £m	2016 Level 3 £m	2016 Total £m
Fair value of financial assets held at amortised cost								
Loans and advances to banks	-	2,779	-	2,779	-	3,349	-	3,349
Loans and advances to customers	-	-	20,031	20,031	-	-	19,841	19,841
Total	**-**	**2,779**	**20,031**	**22,810**	**-**	**3,349**	**19,841**	**23,190**
Fair value of financial liabilities held at amortised cost								
Deposits from banks	-	3,576	-	3,576	-	2,714	-	2,714
Customer accounts	-	18,970	-	18,970	-	19,459	-	19,459
Subordinated liabilities	-	301	-	301	-	351	-	351
Total	**-**	**22,847**	**-**	**22,847**	**-**	**22,524**	**-**	**22,524**

	2017 Level 1 £m	2017 Level 2 £m	2017 Level 3 £m	2017 Total £m	2016 Level 1 £m	2016 Level 2 £m	2016 Level 3 £m	2016 Total £m
Financial assets held at fair value								
Derivative financial instruments	-	27	-	27	-	55	-	55
Loans and advances to banks	-	1	-	1	-	63	-	63
Available for sale financial assets	1,008	-	-	1,008	1,140	-	-	1,140
Non-financial assets held at fair value								
Property held at fair value	-	-	23	23	-	-	7	7
Total assets held at fair value	**1,008**	**28**	**23**	**1,059**	**1,140**	**118**	**7**	**1,265**
As a % of fair value assets	**95%**	**3%**	**2%**	**100%**	**90%**	**9%**	**1%**	**100%**
Financial liabilities held at fair value								
Customer accounts	-	1	-	1	-	63	-	63
Derivative financial instruments	-	65	-	65	-	102	-	102
Total financial liabilities held at fair value	**-**	**66**	**-**	**66**	**-**	**165**	**-**	**165**
As a % of fair value liabilities	**-**	**100%**	**-**	**100%**	**-**	**100%**	**-**	**100%**

The Group had non-financial assets held at fair value on the balance sheet in Level 3 at 31 December 2017 and 31 December 2016 due to the purchase of freehold land and buildings and long leaseholds from the Parent.

Movements in level 3 assets
There were no transfers between levels 1, 2 or 3 during the year ended 31 December 2017 or 31 December 2016.

Property held at fair value	2017 £m	2016 £m
At 1 January	7	7
Additions	15	-
Revaluation of property	1	-
At 31 December	**23**	**7**

35 Fair value of assets and liabilities (continued)

Quantitative information about fair value measurements using significant unobservable inputs (Level 3)

Level 3 assets	Valuation technique	Unobservable input	Fair Value 2017 £m	Fair Value 2016 £m	Range 2017 %	Range 2016 %
Property held at fair value	Market comparable property transactions	Property valuation assumptions	23	7	Third party pricing	Third party pricing

	2017 Carrying amount £m	2017 Fair values £m	2016 Carrying amount £m	2016 Fair values £m
Financial Assets				
Loans and advances to banks	2,764	2,780	3,369	3,412
Loans and advances to customers	19,997	20,031	19,821	19,841
Financial Liabilities				
Deposits from banks	3,561	3,576	2,691	2,714
Customer accounts	18,961	18,971	19,475	19,522
Subordinated liabilities	290	301	335	351

The carrying amount and the fair value of the Group's financial assets and liabilities which are carried at amortised cost are set out in the table. Items where the carrying amount is a reasonable approximation of fair value are not included, as permitted by IFRS 7.

36 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, joint ventures and the Parent, as well as key management personnel.

(a) Parent

The immediate parent and owner of the entire share capital of the Group is The Governor and Company of the Bank of Ireland, a corporation established in Ireland in 1783 under Royal Charter.

During 2017, it was advised by the Single Resoluation Board and the Bank of England that their preferred resolution strategy consisted of a single point of entry bail-in. This required the establishment of a holding company structure at the top of the Bank of Ireland Group. Following shareholder approval, Bank of Ireland Group Plc was listed as the holding company and ultimate parent of the Bank of Ireland Group and Bank of Ireland (UK) Plc. Trading in the new ordinary shares commenced on 10 July 2017. 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 the Bank in its transactions with the Bank of England (including its subsidiary, the Bank of England Asset Purchase Facility Fund Limited). If in any circumstances the Bank 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 may be required to pay the amounts or perform its obligations upon written demand from the 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 including derivatives 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 note 7 of the financial statements.

Other transactions with the Parent in 2017 and 2016

(i) On 18 October 2017 a dividend payment of £160 million was paid to the Parent. (2016: £220 million)

(ii) On 19 December 2017 the Group repaid £135 million of subordinated debt to the Parent. On the same date the Group issued £90 million of Tier 2 subordinated floating rate notes to the Parent (refer to note 29).

On 3 May 2017 a coupon payment of £16 million was paid to the Parent in relation to the £200 million Additional tier 1 instrument (refer to note 32). On 28 November 2017 a coupon payment of £8 million was paid to the Parent in relation to the £100 million Additional tier 1 instrument (refer to note 32).

36 Related party transactions (continued)

(iii) During 2017, the Group continued the process of moving from a gross flow cash hedging model to a derivatives hedging model. As a result, £0.6 billion (2016: £0.6 billion) of balances owed to the Parent and £0.6 billion (2016: £0.5 billion) of balances owed from the Parent were repaid during 2017.

(iv) In April 2017 the Group acquired a 50% interest in a freehold property from the Parent for £15 million.

Summary - Parent[1]	2017 £m	2016 £m
Income statement		
Interest income (note 2)	3	23
Interest expense (note 3)	(36)	(49)
Fees and commissions expense (note 4)	(8)	(7)
Net trading expense (note 5)	9	(18)
Operating expenses paid for services provided[2] (note 7)	(220)	(226)
Total	**(252)**	**(277)**
Assets		
Loans and advances to banks (note 14)	1,394	2,038
Loans and advances to customers (note 16)	6	6
Other assets (note 22)	1	3
Derivatives (note 13)	20	50
Total assets	**1,421**	**2,097**
Liabilities		
Deposits from banks (note 24)	1,989	1,912
Customer accounts (note 25)	8	7
Other liabilities (note 26)	2	8
Derivatives (note 13)	63	89
Subordinated liabilities (note 29)	290	335
Total liabilities	**2,352**	**2,351**
Net exposure	**(931)**	**(254)**

(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 Bank of Ireland Group for the benefit of employees, which are conducted on similar terms to third party transactions.

[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 £52,131 (year ended 31 December 2016: £48,090) to Archie Kane, Governor and Non-executive Director of the Parent who was appointed as consultant advisor to the Group in June 2012.

36 Related party transactions (continued)

Companies Act disclosures Loans to Directors 2017	**Balance as at 1 January 2017[1] £'000**	**Balance as at 31 December 2017[2] £'000**	**Aggregate maximum amount outstanding during the year ended 31 December 2017[3] £'000**
Loans to Directors	2	3	8

Companies Act disclosures Loans to Directors 2016	Balance as at 1 January 2016[4] £'000	Balance as at 31 December 2016[2] £'000	Aggregate maximum amount outstanding during the year ended 31 December 2016[3] £'000
Loans to Directors	23	2	9

(c) 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.

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. They do not involve more than the normal risk of collectability.

ii. Key management personnel - loans and deposits
For the purposes of IAS 24 Related Party Disclosures, 'key management personnel' comprise the Directors of the Board, the COO, the Managing Director Northern Ireland, the Managing Director of AA Business, the Director of Consumer Banking UK, the Interim HR Director, Head of Capability Development and any past KMP, who were a KMP during the relevant year.

KMP, 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.

The aggregate amounts outstanding, in respect of all loans, quasi-loans and credit transactions, between the Group, its KMP (as defined above) and KMP of the Parent, including members of their close families and entities influenced by them are shown in the table.

[1] *The opening balance includes balances and transactions with Directors who have retired during 2016 and are not related parties during the current year. Therefore, these Directors are not included in the maximum amounts outstanding.*
[2] *Balance includes principal and interest.*
[3] *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 any Director is £14,000.*
[4] *Foreign currency amounts are converted to GBP, using exchange rates at 1 January 2016 and the average exchange rate for the year, as appropriate.*

36 Related party transactions (continued)

2017 **Key management personnel**	**Balance as at 1 January 2017[5] £'000**	**Balance as at 31 December 2017[1] £'000**	**Aggregate maximum amounts outstanding during the year ended 31 December 2017[2,3] £'000**	**Total number of KMP as at 1 January 2017**	**Total number of KMP as at 31 December 2017**
Loans	3	65	84	3	7
Deposits	195	109	871	13	11

2016 Key management personnel	Balance as at 1 January 2016[4,5] £'000	Balance as at 31 December 2016[1] £'000	Aggregate maximum amounts outstanding during the year ended 31 December 2016[2,3] £'000	Total number of KMP as at 1 January 2016	Total number of KMP as at 31 December 2016
Loans	25	3	24	5	3
Deposits	569	195	814	14	13

CRD IV Pillar 3 disclosures for the Group also include information on remuneration. This can be found on the website of the Bank of Ireland (UK) plc at www.bankofirelanduk.com.

(d) Compensation of key management personnel	**2017 £m**	2016 £m
Remuneration		
Salaries and other short term benefits	4,007	3,813
Pension benefits	458	451
Total	**4,465**	**4,264**

- Total compensation paid to KMP was £4.5 million for the year ended 31 December 2017 and of this amount £1.6 million was paid to Directors. This compared to £4.3 million and £1.5 million respectively for the comparative year ended 31 December 2016;
- During the year ended 31 December 2017 or the year ended 31 December 2016, 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 2017 was £411,764 comprising salary and other benefits (year ended 31 December 2016: £394,239). The total accrued pension and accrued lump sum of this Director at the year ended 31 December 2017 was £nil;
- One Executive Director accrued retirement benefits under a defined benefit and defined contribution Bank of Ireland Group Pension Scheme for year ended 31 December 2017;
- 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 2017 or the year ended 31 December 2016.

[1] *Balance includes principal and interest.*
[2] *These figures include credit card exposures at the maximum statement balance. In all cases, KMP have not exceeded their approved limits. The maximum approved credit limit on any credit card held by KMP is £14,000.*
[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 2017 for any member of KMP and their close family did not exceed £72,896 (31 December 2016: £9,235). 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 1 January 2016 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. Therefore, these KMP's are not included in the maximum amounts outstanding.*

37 Offsetting financial assets and liabilities

The following items have been offset in the balance sheet, in accordance with paragraph 42 of IAS 32.

In addition, as set out in section 2.1.2 of the Risk management report, the Group's net exposure to the Parent is managed through a contractual master netting agreement with the Parent. These amounts do not meet the criteria for offset under paragraph 42 of IAS 32 and are presented gross within loans and advances to banks, derivatives and deposits by banks respectively. Further detail on these amounts is set out in notes 13, 14 and 24 of the financial statements.

	2017			2016		
Assets	**Gross amounts of recognised financial assets £m**	**Gross amounts of recognised financial liabilities[7] set off in the balance sheet £m**	**Net amounts of financial assets presented in the balance sheet £m**	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	449	(449)	-	648	(648)	-

38 Interests in other entities

Names	**Principal activity**	**Country of incorporation**	**Statutory year end**	**Percentage of ordinary share capital held %**	**Percentage of voting rights held %**
NIIB Group Limited	Personal finance and leasing	Northern Ireland	31 December	100	100
Northridge Finance Limited[1]	Personal finance and leasing	Northern Ireland	31 December	100	100
Bank of Ireland Personal Finance Limited[2]	Personal finance	Northern Ireland	31 December	100	100
Bank of Ireland Trustee Company Limited[3]	Client Investment Services	Northern Ireland	31 December	100	100
Midasgrange Limited[4]	Dormant	England and Wales	30 September	100	100
First Rate Exchange Services Holdings Limited[5]	Foreign Exchange	England and Wales	31 March	50	50
First Rate Exchange Services Limited	Foreign Exchange	England and Wales	31 December	50	50
Marshall Leasing Limited[6]	Commercial Vehicle Leasing	England and Wales	31 December	100	100
Gates Contract Hire Limited[6]	Dormant	England and Wales	31 December	100	100

Copies of the financial statements of these undertakings can be obtained from the relevant addresses listed on page 160.

Management has assessed its involvement in all entities in accordance with the definitions and guidance in:
- IFRS 10: Consolidated Financial Statements;
- IFRS 11: Joint Arrangements;
- IAS 28: Investments in Associates and Joint Ventures; and
- IFRS 12: Disclosure of interests in other entities.

The Group controls an entity when it has power over the entity, is exposed to or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Generally, control or significant influence is identified by the level of ownership of ordinary shares and the level of management involvement in the relevant activities of the entity. However, in the case of 'structured entities', management's judgement is required in determining how the investee should be accounted for.

1 On 15 January 2016 the trade of Northridge Finance Limited was transferred to NIIB Group Limited, which continues to trade under the Northridge Finance brand.
2 On 22 January 2016 the trade of Bank of Ireland Personal Finance Limited was transferred to the Bank.
3 In February 2014 Bank of Ireland Trustee Company Limited ceased to be actively trading.
4 On 3 September 2012 the trade of Midasgrange Limited was transferred to the Bank.
5 This entity is a joint venture with the UK Post Office in which the Group holds 50% of the equity of the company. FRESH holds 100% of the equity in FRES.
6 On 24 November 2017 the Group acquired 100% of Marshall Leasing Limited and its dormant subsidiary, Gates Contract Hire Limited. See note 20 for further details.
7 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

38 Interests in other entities (continued)

Structured entities
A structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. The Group assesses whether it has power over the relevant activities in assessing control over such an entity by considering factors such as who manages the assets of these entities, if the Group has lending to them or has a residual interest in them.

In the case of structured entities, the Group considers it has control over the investee where it is a securitisation vehicle whose purpose is to finance specific loans and advances to customers. In each case the Group considers that it has power over the entity, is exposed to or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

The Group has a structured entity (Bowbell No 1 plc), whose purpose is to acquire mortgage loans and other financial assets and issue mortgage backed securities. This entity is consolidated in the Group's financial statements. All of the assets and liabilities are restricted. The Group does not foresee any significant events or circumstances that could expose it to a loss as a result of its holding in Bowbell No 1 plc.

Total assets amounted to £2.9 billion (31 December 2016: £3.5 billion) and liabilities amounted to £1.2 billion (31 December 2016:£1.6 billion). There are no contractual arrangements that require the Group to provide financial support. In the years ended 31 December 2017 or 31 December 2016 the Group did not provide financial or other support, nor does it expect or intend to do so.

		2017		2016	
Activity	**Company**	**Loans and advances to customers £m**	**Notes in issue £m**	Loans and advances to customers £m	Notes in issue £m
Acquiring mortgage loans and issuing mortgage backed securities	Bowbell No 1 plc	2,886	1,155	3,397	1,560

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.

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.

There are no significant restrictions on the Group's ability to access or use the assets and settle the liabilities of the Group.

39 Post balance sheet events

There are no post balance sheet events that require disclosure in the financial statements.

40 Approval of financial statements

The Board of Directors approved the financial statements on 6 March 2018.

Bank Financial Statements

Independent auditors' report to the members of Bank of Ireland (UK) plc

Report on the audit of the company financial statements

Opinion

In our opinion, Bank of Ireland (UK) plc's company financial statements (the "financial statements"):

- give a true and fair view of the state of the company's affairs as at 31 December 2017 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law); and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Annual Report, which comprise: the bank balance sheet as at 31 December 2017; the bank income statement, the bank statement of comprehensive income, the bank statement of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the company.

Other than those disclosed in note 8 to the financial statements, we have provided no non-audit services to the group and its subsidiaries in the period from 1 January 2017 to 31 December 2017.

Our audit approach

Overview

Materiality

- Overall materiality: £7,600,000, based on 5% of profit before tax.
- The scope of our audit and the nature, timing and extent of the audit procedures performed were determined by our risk assessment, the financial significance of the Bank's reporting components and other qualitative factors.
- We performed full scope audit procedures over components considered to be financially significant. We also performed audit procedures over specific account balances in other components that were significant to the Bank.
- PwC Ireland were essential to this scope carrying out the majority of the audit procedures relating to a number of areas including IT testing.
- Audit coverage for individual line items within the income statement and balance sheet falls in the range of 81% to 100%; most line items have coverage above 90%.
- See page 136 for further details.
- Impairment provision on loans and advances to customers.
- Revenue recognition relating to effective interest rate (EIR) accounting for mortgages and unwind of fair value adjustments on acquired mortgages.
- IT risk.

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

We gained an understanding of the legal and regulatory framework applicable to the company and the industry in which it operates, and considered the risk of acts by the company which were contrary to applicable laws and regulations, including fraud. We designed audit procedures to respond to the risk, recognising that the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. We focused on laws and regulations that could give rise to a material misstatement in the

Our audit approach (continued)

company's financial statements, including, but not limited to, the Companies Act 2006, the Financial Services and Markets Act 2000 and UK tax legislation. Our tests included, but were not limited to, review of the financial statement disclosures to underlying supporting documentation, review of correspondence with the regulators and enquiries of management. There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it.

We did not identify any key audit matters relating to irregularities, including fraud. As in all of our audits we also addressed the risk of management override of internal controls, including testing journals and evaluating whether there was evidence of bias by the directors that represented a risk of material misstatement due to fraud.

Key audit matters

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

Key audit matter	How our audit addressed the key audit matter
Impairment provision on loans and advances to customers Refer to page 142 (Bank Accounting Policies) and pages 142 to 149 (Notes to the Financial Statements). We focused on the identification and determination of provisions in relation to the mortgage and commercial loan portfolios as it requires management to make complex and subjective judgments. In the commercial loan portfolio, individual impairment assessments are performed where there are observed impairment indicators. There is significant judgement required for each loan to determine the level of any provision. Our focus was on the principal assumptions applied by management in estimating the impairment allowance such as the value of collateral and forecast cash flows. For the incurred but not reported (IBNR) and collective specific mortgage provisions we focused on: • The appropriateness of the models used to estimated impairment provisions; • The judgements around the propensities of default and subsequent possession which are based on historic data and customer credit profiles; and • Loss rates determined by expected recoveries focusing on management's assumptions around house price changes and forced sale discounts.	We understood and evaluated the design of key controls over the commercial and mortgage impairment processes and tested their effectiveness. We noted no significant exceptions in these controls. Accordingly, we relied on them for the purposes of our audit. In addition, we performed the substantive procedures described below. *Commercial impairment* For a sample of individually impaired loans, we evaluated the specific circumstances of the borrower, the basis on which the provision was determined and whether key judgements were appropriate. We re-performed management's discounted cash flow forecast calculations, testing key inputs such as expected future cash flows and discount rates. We tested the valuation of collateral held and challenged management on subjective estimates and assumptions. We also compared gains and losses realised when a loan is sold or exited to the existing provision. Based on the procedures performed and the evidence obtained, we found management's methodology, assumptions and judgments to be reasonable. *Mortgage impairment* We assessed the appropriateness of key assumptions used in the modelling by comparing against recent group experience as well as our industry experience. We tested the completeness and accuracy of underlying data sources into the impairment models. We reviewed the coding used in the model for the calculation of the provisions and the calculation of key model inputs. We performed sensitivity analyses in order to identify higher risk assumptions and inputs which included default and possession propensities and loss rates. In these areas we performed additional targeted procedures and we concluded that the assumptions and inputs used were reasonable.

Our audit approach (continued)

Key audit matter	How our audit addressed the key audit matter
Revenue recognition relating to effective interest rate (EIR) accounting for mortgages and unwind of fair value adjustments on acquired mortgages Refer to page 142 (Bank Accounting Policies) and pages 142 to 159 (Notes to the Financial Statements). The Bank's total loans and advances to customers balance of £20.3 billion and net interest income of £433 million include certain manual adjustments that involve management judgment. The vast majority of the Bank's income is system generated and requires minimal judgment, therefore we focused our work in relation to the risk of fraud in revenue recognition on adjustments relating to mortgage EIR and the unwind of fair value adjustments linked to the acquisition of mortgages. Changes in the assumptions used in the associated models could have a material impact on the revenue recognised in any one accounting period. We focused on the most significant judgment for mortgage EIR which is the estimation of the expected life of the mortgage over which the associated fees, costs and discounts are spread. In relation to the unwind of fair value adjustments linked to acquired mortgages, we focused on significant judgment management make in assessing rates of future customer redemptions, particularly relating to but-to-let mortgages.	Across both the mortgage EIR and fair value unwind models, we tested controls over the assumptions used and checked the accuracy of model calculations by reviewing formulas used and considering whether these were in line with our expectations. For mortgage EIR we: • substantively tested a sample of fees, costs and interest rates back to underlying lending agreements and source documentation; • assessed the estimate of the expected mortgage life applied and forecast cash flows during this life by comparing to recent group experience and expectations of future patterns. For fair value unwind we: • tested the accuracy of data inputs into the model; • agreed redemption assumptions applied in the model to those that were approved by management and considered the reasonableness of the assumptions. We evaluated whether the disclosures made in the financial statements were sufficiently clear in describing the key assumptions and their sensitivity. We concluded that whilst there is significant judgment inherent in the mortgage EIR and fair value unwind adjustments, the assumptions applied were within a reasonable range based on past experience and future assumptions. We concluded the disclosures provided appropriate detail of the estimation uncertainty and the impact of actual future customer experience differing from the assumptions made.

Our audit approach (continued)

Key audit matter	How our audit addressed the key audit matter
IT risk The Bank has a complex IT environment and operates a number of IT applications to support its business activities. A significant number of these applications (whether developed by management or purchased from third party vendors) have been in place for many years. There is a mix of automated and manual interfaces between applications. The IT control framework over financial reporting includes standardised IT general controls most of which relate to a number of applications, designed to prevent or detect material misstatements in the recording, processing and reporting of financial information. The Bank invests to maintain the operating effectiveness of the IT systems as well as managing other factors including increased expectations from regulators and customers. Bank of Ireland Group Internal Audit ("GIA") has reported on the related internal control and operational risk considerations. Management has an ongoing risk management programme in place to identify, rate, mitigate and report on risk including IT and Operational risk considerations. We focused on this area because the Bank's business is highly IT dependent, the IT environment is complex and the design and operating effectiveness of IT controls and of IT risk mitigants supports the financial reporting process.	Due to the structure of the Bank of Ireland Group, the key IT processes are based in Dublin and as such, the majority of the audit work was performed by PwC Ireland, in Dublin. We remained responsible for the overall scoping of the audit work, as well as the reporting of findings and results relevant to the Bank. Throughout the audit relevant findings identified by PwC Ireland were reported to us so we could determine the impact on our audit approach and opinion. Using principally PwC Ireland IT audit specialists, we updated our understanding of the Bank's IT environment and of changes made to it during 2017. In particular, we considered the outputs from management's IT risk management process and the findings of reviews conducted by GIA. We considered the impact of the assessed risks on our audit approach. We considered those IT risks and significant GIA IT audit issues that management assessed as relevant to financial reporting and tested and challenged management's assessment of the mitigation of these risks relevant to financial reporting. We also considered management's documentation and testing of the design and operating effectiveness of the IT controls within the Bank of Ireland Group's Internal Control Framework over financial reporting and tested the design and operating effectiveness of those controls upon which we wished to rely. Where relevant, we considered whether compensating controls acted as effective mitigants of design or operating deficiencies identified by management or us. In the absence of sufficient compensating controls, we examined, tested and challenged management's documented assessments of the risk which control deficiencies posed to the financial reporting process. We concluded following completion of our audit procedures that management's assessments of the impact of IT risk matters on the financial reporting process were reasonable and that we could place reliance on the operation of in-scope IT systems and reports generated from them.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the company, the accounting processes and controls, and the industry in which it operates.

The Bank comprises fifteen components through which it reports its operating results and financial position of which four are significant to our audit. These are Mortgages, Business Banking, Post Office Financial Services and Divisional Centre. The components report through an integrated consolidation system. We identified the components which, in our view, required a full scope audit either due to their size or their risk characteristics in the context to the Bank's financial statements.

In order to achieve the desired level of audit evidence on each account balance in the financial statements, we identified six further reporting units that we determined to be individually significant in respect of one or more account balances and performed specific audit procedures over those account balances. Specific audit procedures were performed on credit cards and ATM income and expense.

Processes supporting the Bank's operations are also performed at a Bank of Ireland Group plc level in the Republic of Ireland, including the hosting and monitoring of the IT systems used by the Bank. As part of the planning and execution of the audit, we visited the auditor of the parent, held regular physical and telephone meetings throughout the audit and reviewed extracts from PwC Ireland's audit file to corroborate that the procedures performed on our behalf were sufficient for our purposes.

Together with additional procedures performed at the Group level, this gave us the evidence we needed for our opinion on the financial statements as a whole.

Audit coverage for individual line items within the income statement and balance sheet falls in the range of 81% to 100%; most line items have coverage above 90%.

Our audit approach (continued)

Materiality
The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Bank of Ireland (UK) financial statements
Overall materiality £7.6 million
How we determined it 5% of profit before tax.
Rationale for benchmark applied We believe that profit before tax is the primary measure used by the shareholders in assessing the performance of the Bank, and is a generally accepted auditing benchmark.
We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £375,000 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern
We have nothing to report in respect of the following matters in relation to which ISAs (UK) require us to report to you when:
- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the company's ability to continue as a going concern.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Report of the Directors, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, ISAs (UK) require us also to report certain opinions and matters as described below.

Strategic Report and Report of the Directors
In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Report of the Directors for the year ended 31 December 2017 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Report of the Directors.

Responsibilities for the financial statements and the audit

Responsibilities of the Directors for the financial statements
As explained more fully in the Statement of Directors' Responsibilities set out on page 71, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

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

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report..

Use of this report
This report, including the opinions, has been prepared for and only for the company'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.

Other required reporting

Companies Act 2006 exception reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion:
- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the audit committee, we were appointed by the directors on 9 July 2010 to audit the financial statements for the period ended 31 March 2010 and subsequent financial periods. The period of total uninterrupted engagement is 7.5 years, covering the periods ended 31 March 2010 to 31 December 2017.

Other matter

We have reported separately on the group financial statements of Bank of Ireland (UK) plc for the year ended 31 December 2017.

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

6 March 2018

Bank Financial Statements and Notes

Bank income statement *(for the year ended 31 December 2017)*

	2017 £m	2016 £m
Interest income	614	729
Interest expense	(181)	(267)
Net interest income	**433**	**462**
Fee and commission income	113	118
Fee and commission expense	(115)	(121)
Net trading expense	(1)	(5)
Other operating income	56	61
Total operating income	**486**	**515**
Operating expenses	(314)	(301)
Operating profit before impairment charges on financial assets	**172**	**214**
Impairment charges on financial assets	(24)	(22)
Operating profit	**148**	**192**
Profit before taxation	**148**	**192**
Taxation charge	(17)	(26)
Profit for the year	**131**	**166**

Bank statement of other comprehensive income *(for the year ended 31 December 2017)*

	2017 £m	2016 £m
Profit for the year	**131**	**166**
Items that may be reclassified to profit or loss in subsequent periods		
Net change in cash flow hedge reserve (net of tax)[1]	(9)	21
Net change in available for sale reserve (net of tax)[2]	-	3
Total items that may be reclassified to profit or loss in subsequent periods	**(9)**	**24**
Items that will not be reclassified to profit or loss in subsequent periods		
Net change in revaluation reserve, net of tax	1	-
Total items that will not be reclassified to profit or loss in subsequent periods	**1**	**-**
Other comprehensive income / (expense) for the year, net of tax	**(8)**	**24**
Total comprehensive income for the year, net of tax	**123**	**190**

[1] *Net of tax credit £3 million (2016: charge £7 million).*
[2] *Net of tax £0.4 million (2016: £1 million).*

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Bank balance sheet *(as at 31 December 2017)*

	Note	2017 £m	2016 £m
Assets			
Cash and balances at central banks	c	1,836	1,172
Items in the course of collection from other banks		192	131
Derivative financial instruments	d	27	55
Loans and advances to banks	e	2,625	3,221
Available for sale financial assets	f	1,008	1,140
Loans and advances to customers	g	20,289	20,043
Investment in subsidiaries	i	8	8
Interest in joint venture		2	2
Intangible assets	j	19	24
Property, plant and equipment	k	23	7
Other assets	l	102	109
Deferred tax assets	r	65	63
Total assets		**26,196**	**25,975**
Equity and liabilities			
Deposits from banks	n	3,554	2,675
Customer accounts	o	19,045	19,604
Items in the course of transmission to other banks		108	85
Derivative financial instruments	d	65	102
Current tax liabilities		3	6
Other liabilities	p	1,217	1,195
Provisions	q	12	15
Subordinated liabilities	s	290	335
Total liabilities		**24,294**	**24,017**
Equity			
Share capital	u	851	851
Retained earnings		157	204
Other reserves		594	603
Other equity instruments	v	300	300
Total equity		**1,902**	**1,958**
Total equity and liabilities		**26,196**	**25,975**

The financial statements on pages 139 to 159 were approved by the Board on 6 March 2018 and were signed on its behalf by:

Thomas McAreavey

Thomas McAreavey
Director
6 March 2018

Company Number: 07022885

Bank statement of changes in equity *(for the year ended 31 December 2017)*

	2017 £m	2016 £m
Share capital		
Balance at 1 January	851	851
Balance at 31 December	**851**	**851**
Retained earnings		
Balance at 1 January	204	277
Profit for the year	131	166
Dividend on ordinary shares	(160)	(220)
Distribution on other equity instruments - Additional tier 1 coupon, net of tax[1]	(18)	(19)
Balance at 31 December	**157**	**204**
Other equity instruments		
Balance at 1 January	300	300
Balance at 31 December	**300**	**300**
Other reserves:		
Available for sale reserve		
Balance at 1 January	5	2
Changes in fair value, net of hedge accounting adjustments	(1)	9
Transfer to income statement (pre tax)	-	(5)
Deferred tax on reserve movements	-	(1)
Balance at 31 December	**4**	**5**
Revaluation reserve - property		
Balance at 1 January	-	-
Revaluation of property	1	-
Balance at 31 December	**1**	**-**
Cash flow hedge reserve		
Balance at 1 January	32	11
Changes in fair value	3	43
Transfer to income statement (pre tax)	(15)	(15)
Deferred tax on reserve movements	3	(7)
Balance at 31 December	**23**	**32**
Capital contribution		
Balance at 1 January	266	266
Balance at 31 December	**266**	**266**
Capital redemption reserve fund		
Balance at 1 January	300	300
Balance at 31 December	**300**	**300**
Total other reserves	**594**	**603**
Total equity	**1,902**	**1,958**
Included in the above:		
Total comprehensive income for the year, net of tax	**123**	**190**

[1] *The Additional tier 1 coupon paid to the Parent of £18 million (2016: £19 million) is presented net of the related tax credit of £6 million (2016: £5 million), comprising £5 million (2016: £3 million) relating to current tax and £1 million (2016: £2 million) relating to deferred tax.*

Notes to the Bank financial statements

a Basis of preparation and 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 and the notes to the Bank financial statements.

The Bank meets the definition of a qualifying entity under FRS 100 (Financial Reporting Standard 100) issued by the Financial Reporting Council. Accordingly, in the year ended 31 December 2017 the Bank has undergone transition from reporting under IFRSs adopted by the European Union to FRS 101 as issued by the Financial Reporting Council. The financial statements for the year ended 31 December 2017 have therefore been prepared in accordance with the Companies Act 2006 as applicable to companies using FRS 101 'Reduced disclosure framework'. This transition had no measurement impact on the financial statements.

These financial statements are financial statements of the Bank only and do not consolidate the results of any subsidiaries.

In preparing these financial statements the Bank applies the recognition, measurement and disclosure requirements of IFRS as adopted by the EU. The Bank has applied the exemptions available under FRS 101 in respect of the following disclosures:

- statement of cash flows; and
- disclosures in respect of transactions with wholly-owned subsidiaries.
- certain requirements of IAS 1 'Presentation of financial statements'; and
- the effects of new but not yet effective IFRSs.

The financial statements have been prepared under the historical cost convention, as modified to include the fair valuation of certain financial instruments and properties. The accounting policies and critical accounting estimates and judgements of the Bank are the same as those of the Group which are set out in the Group accounting policies section on pages 84 to 98, where applicable.

The preparation of financial statements in conformity with FRS 101 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 period. 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 97 to 98 in the accounting policies section.

Information on risk management and capital management is included in the Risk Management Report, with certain financial information specific to the Bank being included in notes m and w respectively.

b Auditors' remuneration

Information on auditors' remuneration is set out in note 8 to the Consolidated financial statements.

c Cash and cash equivalents

Cash and cash equivalents	2017 £m	2016 £m
Cash	30	31
Balances with central banks	1,806	1,141
Total cash balances included in cash and cash equivalents	**1,836**	**1,172**
Loans and advances to banks	2,625	3,221
Less: amounts with a maturity of three months or more	(960)	(1,542)
Total loans and advances to banks included in cash and cash equivalents	**1,665**	**1,679**
Total cash and cash equivalents	**3,501**	**2,851**
Due from the Parent	424	484

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d Derivative financial instruments

	2017			2016		
		Fair values			Fair values	
	Contract notional amounts £m	**Assets £m**	**Liabilities £m**	Contract notional amounts £m	Assets £m	Liabilities £m
Derivatives held for trading						
Foreign exchange derivatives						
Currency forwards	156	3	1	176	3	8
Currency forwards – with the Parent	156	1	3	176	8	3
Currency swaps	207	4	1	166	2	5
Currency swaps - with the Parent	207	1	4	167	5	2
Total foreign exchange derivatives held for trading	**726**	**9**	**9**	**685**	**18**	**18**
Interest rate derivatives						
Interest rate swaps - with the Parent	2,064	3	2	1,677	5	2
Cross currency interest rate swaps - with the Parent	104	-	-	117	-	-
Total interest rate derivatives held for trading	**2,168**	**3**	**2**	**1,794**	**5**	**2**
Total derivatives held for trading	**2,894**	**12**	**11**	**2,479**	**23**	**20**
Derivatives held as fair value hedges						
Interest rate swaps - with the Parent	4,061	9	41	5,023	6	75
Derivatives held as cash flow hedges						
Interest rate swaps - with the Parent	3,590	6	13	2,950	26	7
Total derivative assets / liabilities held for hedging	**7,651**	**15**	**54**	**7,973**	**32**	**82**
Total derivative assets / liabilities	**10,545**	**27**	**65**	**10,452**	**55**	**102**

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

2017	**Up to 1 year £m**	**1-2 years £m**	**2-5 years £m**	**Over 5 years £m**	**Total £m**
Forecast receivable cash flows	5	8	34	16	63
Forecast payable cash flows	(11)	(14)	(4)	-	(29)

2016	Up to 1 year £m	1-2 years £m	2-5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	5	4	26	16	51
Forecast payable cash flows	(1)	(1)	(2)	-	(4)

d Derivative financial instruments (continued)

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

2017	**Up to 1 year £m**	**1-2 years £m**	**2-5 years £m**	**Over 5 years £m**	**Total £m**
Forecast receivable cash flows	6	9	34	14	63
Forecast payable cash flows	(12)	(13)	(4)	-	(29)

2016	Up to 1 year £m	1-2 years £m	2-5 years £m	Over 5 years £m	Total £m
Forecast receivable cash flows	5	5	27	14	51
Forecast payable cash flows	(1)	(1)	(2)	-	(4)

During the years ended 31 December 2017 and 31 December 2016, there were no forecast transactions to which the Group had applied hedge accounting which were no longer expected to occur.

e Loans and advances to banks

	2017 £m	2016 £m
Placements with other banks	1,402	2,043
Mandatory deposits with central banks	1,223	1,178
Loans and advances to banks	**2,625**	**3,221**
Amounts include:		
Due from the Parent	1,383	2,027

Represented in placements with other banks are:

- an amount of £1,383 million (31 December 2016: £2,027 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 £1,982 million (31 December 2016: £1,896 million) are also disclosed in note n. From a counterparty credit risk perspective, while 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
- £1 million of loans included in amounts due from the Parent, whose return is dependent on movements in various external indices (31 December 2016: £63 million). These loans are designated at fair value through profit or loss. Refer to note x for details on fair value.

During the year ended 31 December 2017, £0.6 billion of balances were repaid by the Parent. For further details, refer to note 36 in the consolidated financial statements.

Represented in mandatory deposits with central banks are:

- an amount of £1,189 million relating to collateral with the Bank of England in respect of notes in circulation (31 December 2016: £1,142 million). £683 million of this refers to non-interest bearing collateral (31 December 2016: £644 million); and
- an amount of £34 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 2016: £36 million).

f Available for sale financial assets

	2017 £m	2016 £m
Government bonds	428	585
Debt securities listed	580	555
Available for sale financial assets	**1,008**	**1,140**

At 31 December 2017 and at 31 December 2016, no available for sale financial assets were pledged in sale and repurchase agreements.

Movements on available for sale financial assets	2017 £m	2016 £m
At 1 January	1,140	956
Revaluation adjustments	(12)	20
Additions	82	301
Redemptions / disposals	(198)	(133)
Amortisation	(4)	(4)
At 31 December	**1,008**	**1,140**

g Loans and advances to customers

	2017 £m	2016 £m
Residential mortgages	16,043	15,964
Non-property SME and corporate	2,786	2,624
Commercial property and construction	652	961
Consumer	952	750
Gross loans and advances to customers	**20,433**	**20,299**
Less: allowance for impairment charges on loans and advances to customers (note h)	(144)	(256)
Loans and advances to customers	**20,289**	**20,043**
Amounts include:		
Due from subsidiaries	1,760	1,512
Due from entities controlled by the Parent	6	6

Refer to note 16 in the consolidated financial statements for further details.

h Impairment provisions

2017	**Residential mortgages £m**	**Non-property SME and corporate £m**	**Commercial property and construction £m**	**Consumer £m**	**Total impairment provisions £m**
Provision at 1 January 2017	28	57	152	19	256
Transfer between provisions	-	-	-	-	-
Exchange adjustments	-	1	1	-	2
Provisions utilised	(2)	(31)	(106)	(14)	(153)
Recoveries	(1)	2	5	4	10
Other movements	-	1	3	1	5
Charge to the income statement	2	1	8	13	24
Provision at 31 December 2017	**27**	**31**	**63**	**23**	**144**

2016	Residential mortgages £m	Non-property SME and corporate £m	Commercial property and construction £m	Consumer £m	Total impairment provisions £m
Provision at 1 January 2016	30	91	295	27	443
Transfer between provisions	-	-	-	-	-
Exchange adjustments	-	3	8	-	11
Provisions utilised	(3)	(40)	(176)	(17)	(236)
Recoveries	-	1	3	5	9
Other movements	(1)	2	5	1	7
Charge to the income statement	2	-	17	3	22
Provision at 31 December 2016	28	57	152	19	256

i Investment in subsidiaries

Investment in subsidiaries	**2017 £m**	2016 £m
At 1 January	8	9
Repayment of investment	-	(1)
At 31 December	**8**	**8**

Impairment review
The Bank's investment 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 2017 or the year ended 31 December 2016.

Repayment of capital
During 2016 the Bank received a repayment of capital of £1 million from Midasgrange Limited.

The interests in all entities held by the Group is disclosed in note 38.

j Intangible assets

	2017			2016		
	Computer software internally generated £m	**Other externally purchased intangible assets £m**	**Total £m**	Computer software internally generated £m	Other externally purchased intangible assets £m	Total £m
Cost						
At 1 January	34	76	110	34	76	110
Additions	-	-	-	-	-	-
At 31 December	**34**	**76**	**110**	**34**	**76**	**110**
Accumulated amortisation						
At 1 January	(34)	(52)	(86)	(34)	(46)	(80)
Charge to the income statement	-	(5)	(5)	-	(6)	(6)
At 31 December	**(34)**	**(57)**	**(91)**	**(34)**	**(52)**	**(86)**
Net book value at 31 December	**-**	**19**	**19**	**-**	**24**	**24**

Refer to note 19 in the consolidated financial statements for further details.

k Property, plant and equipment

Property, plant and equipment	**2017 £m**	2016 £m
At 1 January	7	7
Additions	15	-
Revaluation adjustments	1	-
At 31 December	**23**	**7**

Refer to note 21 in the consolidated financial statements for further details.

l Other assets

Other assets	**2017 £m**	2016 £m
Sundry and other receivables	51	51
Accounts receivable and prepayments	32	36
Interest receivable	19	22
Other assets	**102**	**109**
Amount include		
Due from the Parent	1	3
Maturity profile of other assets		
Amounts receivable within 1 year	85	88
Amounts receivable after 1 year	17	21

m 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).

2017	**Residential mortgages £m**	**Non-property SME and corporate £m**	**Commercial property and construction £m**	**Consumer £m**	**Total loans and advances to customers £m**	**Total loans and advances to customers %**
High quality	15,583	136	116	925	16,760	82%
Satisfactory quality	23	2,347	180	-	2,550	12%
Acceptable quality	38	169	95	-	302	2%
Lower quality but not past due nor impaired	-	48	88	-	136	1%
Neither past due nor impaired	**15,644**	**2,700**	**479**	**925**	**19,748**	**97%**
Past due but not impaired	332	37	39	14	422	2%
Impaired	67	49	134	13	263	1%
Total	**16,043**	**2,786**	**652**	**952**	**20,433**	**100%**

2016	Residential mortgages[1] £m	Non-property SME and corporate £m	Commercial property and construction £m	Consumer £m	Total loans and advances to customers £m	Total loans and advances to customers %
High quality	15,483	233	110	728	16,554	82%
Satisfactory quality	20	2,096	221	-	2,337	12%
Acceptable quality	42	99	137	-	278	1%
Lower quality but not past due nor impaired	-	84	175	-	259	1%
Neither past due nor impaired	15,545	2,512	643	728	19,428	96%
Past due but not impaired[2]	352	33	51	13	449	2%
Impaired[2]	67	79	267	9	422	2%
Total	15,964	2,624	961	750	20,299	100%

At 31 December 2017 included in the non-property SME and corporate book is £1,766 million (31 December 2016: £1,518 million) in relation to intra-group funding balances with the Bank's subsidiaries with no banking license, the largest balance being £1,560 million (31 December 2016: £1,378 million) relating to balances with NIIB. All of these balances were classified as satisfactory quality.

[1] *As described on pages 42 and 43, the Group has revised its asset quality reporting methodology to align with EBA guidance on non-performing and forborne classifications. As a result, the Group has amended the risk profile of Residential mortgages which are neither 'past due nor impaired' to reflect this change in classification and comparative figures have been restated resulting in an increase in the 'high quality' by £48 million from £15,435 million with offsetting decreases in 'satisfactory quality' by £5 million from £25 million, 'acceptable quality' by £31 million from £73 million and 'lower quality' by £12 million from £12 million, with no change to the overall total of 'neither past due nor impaired' loans.*

[2] *As described on pages 42 and 43, the Group has modified its definition of impaired loans with a corresponding impact on amounts classified as 'past due greater than 90 days but not impaired'. As a result comparative figures have been restated as follows; impaired 'Non-property SME and corporate' have reduced by £20 million (from £99 million to £79 million) with a corresponding increase in amounts classified as 'past due but not impaired' (from £13 million to £33 million) and impaired 'Commercial property and construction' loans have reduced by £22 million (from £289 million to £267 million) with a corresponding increase in amounts classified as 'past due but not impaired' (from £29 million to £51 million)*

m Credit risk exposures (continued)

Financial assets - 'past due but not impaired': loans and advances to customers
The tables below provide an aged analysis of loans and advances to customers 'past due but not impaired' by asset classification.

2017	**Residential mortgages £m**	**Non-property SME and corporate £m**	**Commercial property and construction £m**	**Consumer £m**	**Total £m**
Past due up to 30 days	107	5	1	11	124
Past due 31-60 days	145	7	21	2	175
Past due 61-90 days	29	2	2	1	34
Past due more than 90 days but not impaired	51	23	15	-	89
Total	**332**	**37**	**39**	**14**	**422**

2016	Residential mortgages £m	Non-property SME and corporate £m	Commercial property and construction £m	Consumer £m	Total £m
Past due up to 30 days	97	5	3	9	114
Past due 31-60 days	159	3	17	2	181
Past due 61-90 days	37	5	9	2	53
Past due more than 90 days but not impaired[1]	59	20	22	-	101
Total	352	33	51	13	449

Financial assets - 'impaired': loans and advances to customers
The tables below provide an analysis of 'impaired' loans and advances to customers by asset classification.

2017	**Advances £m**	**Impaired loans £m**	**Impaired loans as % of advances %**	**Specific provisions £m**	**Specific provisions as % of impaired loans %**
Residential mortgages	16,043	67	-	7	10%
Non-property SME and corporate	2,786	49	2%	25	51%
Commercial property and construction	652	134	21%	59	44%
Consumer	952	13	1%	10	77%
Total	**20,433**	**263**	**1%**	**101**	**38%**

2016	Advances £m	Impaired loans[1] £m	Impaired loans as % of advances %	Specific provisions £m	Specific provisions as % of impaired loans %
Residential mortgages	15,964	67	-	8	12%
Non-property SME and corporate	2,623	79	3%	49	62%
Commercial property and construction	962	267	28%	140	52%
Consumer	750	9	1%	8	89%
Total	20,299	422	2%	205	49%

[1] *Comparative figures have been restated as set out on pages 42 and 43.*

m Credit risk exposures (continued)

	2017 £m	2016 £m
Specific provisions	101	205
Incurred but not reported (IBNR)	43	51
Total impairment provision	**144**	**256**

Impairment provision
The tables split out the impairment provisions and impairment charge by nature and composition.

	2017			2016		
	Specific £m	IBNR £m	Total £m	Specific £m	IBNR £m	Total £m
Residential mortgages	1	1	2	3	(1)	2
Non-property SME and corporate	4	(3)	1	7	(7)	-
Commercial property and construction	15	(7)	8	20	(3)	17
Consumer	11	2	13	4	(1)	3
Total loan impairment charge	**31**	**(7)**	**24**	**34**	**(12)**	**22**

Other financial instruments with ratings equivalent to:	2017 £m	2016 £m
Aaa to Aa3	2,233	2,328
A1 to A3	22	12
Baa1 to Baa3	1,405	2,076
Total	**3,660**	**4,416**

Asset quality: other financial instruments
Other financial instruments include available for sale assets, derivative financial instruments and loans and advances to banks.

Refer to the Risk Management section for further details on Asset quality: other financial instruments page 49.

n Deposits from banks

	2017 £m	2016 £m
Deposits from banks	**3,554**	**2,675**
Amounts include:		
Due to the Parent	1,982	1,896

Deposits from banks includes £1,200 million (31 December 2016: £600 million) of borrowings under the Bank of England Term Funding Scheme, which is collateralised with mortgage loans, and £350 million (31 December 2016: £155 million) borrowed under the Bank of England Indexed Long - Term Repo scheme, which is collateralised with notes issued by Bowbell (see note 38). Refer to note 24 of the consolidated accounts for further information.

Amounts due to the Parent of £1,982 million (31 December 2016: £1,896 million) primarily 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 36 of the consolidated financial statements in respect of changes in these balances during 2017.

o Customer accounts

Customer accounts	2017 £m	2016 £m
Term deposits	6,574	8,900
Demand deposits	9,614	8,145
Non-interest bearing current accounts[1]	2,502	2,191
Interest bearing current accounts	355	368
Customer accounts	**19,045**	**19,604**
Amounts include:		
Due to subsidiaries	84	129
Due to entities controlled by the Parent	8	7

Term deposits include deposits of £1 million (31 December 2016: £63 million), whose return is dependent on movements in various external indices; these deposits are designated at fair value through profit or loss.

p Other liabilities

Other liabilities	2017 £m	2016 £m
Notes in circulation	1,084	1,036
Accrued interest payable	52	78
Sundry payables	66	68
Accruals and deferred income	15	13
Other liabilities	**1,217**	**1,195**
Amounts include:		
Due to the Parent	2	8
Maturity profile of other liabilities		
Amounts payable within 1 year	1,217	1,195

The Bank is authorised to issue banknotes in Northern Ireland under the Bank of Ireland (UK) plc Act 2012.

q Provisions

Provisions	FSCS £m	Other £m	Total £m
At 1 January	5	10	15
Net charge to the income statement	-	11	11
Utilised during the year	(3)	(11)	(14)
At 31 December	**2**	**10**	**12**
Expected utilisation period			
Used within 1 year	2	9	11
Used after 1 year	-	1	1

Financial services compensation scheme
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 ongoing 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 provision at 31 December 2017 represents the Bank's estimate of the interest element of the levy due for the FSCS levy year from 1 April 2017 to 31 March 2018. This is calculated based on the Bank's share of industry protected deposits at 31 December 2016.

The charge to the income statement for 2017 of £2 million has been offset by a write back of opening provision of £2 million.

Other
As at 31 December 2017 a provision of £6 million has been made for certain commissions payable to the Post Office. In addition, as at 31 December 2017 the Bank has a provision of £4 million to cover potential payments to customers in relation to various compliance matters. The provision is based upon management's current expectations of future payments to be made to customers.

[1] *In the comparatives an amount of £126 million was reallocated from Non-interest bearing current accounts to Term deposits.*

r Deferred tax

	2017 £m	2016 £m
The movement on the deferred tax account is as follows:		
At 1 January	63	80
Income statement charge for year	(2)	(11)
Available for sale securities - charge to other comprehensive income	-	(1)
Cash flow hedges - (charge) / credit to other comprehensive income	3	(7)
Additional tier 1 - credit to equity	1	2
Other	-	-
At 31 December	**65**	**63**
Deferred tax assets and liabilities are attributable to the following items:		
Deferred tax assets		
Unutilised tax losses	74	76
Fixed / leased assets	1	1
Total deferred tax assets	**75**	**77**
Deferred tax liabilities		
Cash flow hedges - transferred to reserves	(8)	(11)
Available for sale securities	(1)	(2)
Deferred tax on property held at fair value	(1)	(1)
Total deferred tax liabilities	**(10)**	**(14)**
Represented on the balance sheet as follows:		
Deferred tax assets	**65**	**63**

s Subordinated liabilities

	2017 £m	2016 £m
£90 million subordinated floating rate loans 2022	-	90
£45 million subordinated floating rate loans 2022	-	45
£200 million subordinated floating rate loans 2025	200	200
£90 million subordinated floating rate loans 2027	90	-
Subordinated liabilities	**290**	**335**

Refer to note 29 of the consolidated financial statements for further details.

t Contingent liabilities and commitments

	2017 £m	2016 £m
Contingent liabilities		
Guarantees and irrevocable letters of credit	9	9
Other contingent liabilities	5	5
Total contingent liabilities	**14**	**14**
Commitments		
Undrawn formal standby facilities, credit lines and other commitments to lend		
- revocable or irrevocable with original maturity of 1 year or less	4,205	3,480
- irrevocable with original maturity of over 1 year	47	173
Total commitments	**4,252**	**3,653**

The table sets out 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.

Refer to note 30 of the consolidated financial statements for further details.

u Share capital

	Ordinary Shares[1]	
	2017 £m	2016 £m
At 1 January and 31 December	851	851

Refer to note 31 of the consolidated financial statements for further details.

v Other equity instruments

	2017 £m	2016 £m
At 1 January and 31 December	300	300

Other equity instruments consist of Additional tier 1 securities held by the Parent:

- £200 million issued on 1 May 2015;
- £100 million issued on 26 November 2015

Refer to note 32 of the consolidated financial statements for further details.

[1] *All shares issued are in denominations of £1, therefore the table above also represents unit values.*

w Liquidity risk

The tables below summarise the maturity profile of the Bank's financial liabilities at 31 December 2017 and at 31 December 2016, 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 shown below 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'.

2017 **Maturity profile of financial liabilities**	**Demand £m**	**0-3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Deposits from banks	308	155	1,242	1,865	45	3,615
Customer accounts	14,041	2,053	2,459	582	-	19,135
Subordinated liabilities	-	3	9	53	339	404
Contingent liabilities	14	-	-	-	-	14
Commitments	3,218	-	987	47	-	4,252
Total	**17,581**	**2,211**	**4,697**	**2,547**	**384**	**27,420**

2016 Maturity profile of financial liabilities	Demand £m	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Deposits from banks	333	162	439	1,737	58	2,729
Customer accounts	12,956	2,613	3,239	928	2	19,738
Subordinated liabilities	-	7	16	98	391	512
Contingent liabilities	14	-	-	-	-	14
Commitments	3,054	-	426	173	-	3,653
Total	16,357	2,782	4,120	2,936	451	26,646

The table below summarises the maturity profile of the Bank's derivative liabilities. The undiscounted cash flows payable on derivatives liabilities are classified according to their contractual maturity.

2017 **Maturity profile of derivative liabilities**	**Demand £m**	**0-3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Gross settled derivative liabilities - outflows	(11)	(210)	(197)	(16)	-	(434)
Gross settled derivative liabilities - inflows	11	205	193	16	-	425
Gross settled derivative liabilities - net flows	-	(5)	(4)	-	-	(9)
Net settled derivative liabilities	-	(7)	(11)	(31)	(4)	(53)
Total derivatives cash flows	**-**	**(12)**	**(15)**	**(31)**	**(4)**	**(62)**

2016 Maturity profile of derivative liabilities	Demand £m	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Gross settled derivative liabilities - outflows	(20)	(203)	(141)	(11)	-	(375)
Gross settled derivative liabilities - inflows	20	192	134	11	-	357
Gross settled derivative liabilities - net flows	-	(11)	(7)	-	-	(18)
Net settled derivative liabilities	-	(10)	(19)	(48)	(5)	(82)
Total derivatives cash flows	-	(21)	(26)	(48)	(5)	(100)

x Measurement basis of financial assets and financial liabilities

2017	At fair value through profit or loss: Derivatives designated as fair value hedging instruments £m	At fair value through profit or loss: Held for trading £m	At fair value through profit or loss: Designated upon initial recognition £m	At fair value through Other Comprehensive income (OCI): Available for sale £m	At fair value through Other Comprehensive income (OCI): Cash flow hedge derivatives £m	Held at amortised cost £m	Total £m
Financial assets							
Cash and balances with central banks	-	-	-	-	-	1,836	1,836
Items in the course of collection from other banks	-	-	-	-	-	192	192
Derivative financial instruments	9	12	-	-	6	-	27
Loans and advances to banks	-	-	1	-	-	2,624	2,625
Available for sale financial assets	-	-	-	1,008	-	-	1,008
Loans and advances to customers	-	-	-	-	-	20,289	20,289
Total financial assets	**9**	**12**	**1**	**1,008**	**6**	**24,941**	**25,977**
Financial liabilities							
Deposits from banks	-	-	-	-	-	3,554	3,554
Customer accounts	-	-	1	-	-	19,044	19,045
Items in the course of transmission to other banks	-	-	-	-	-	108	108
Derivative financial instruments	41	11	-	-	13	-	65
Subordinated liabilities	-	-	-	-	-	290	290
Total financial liabilities	**41**	**11**	**1**	**-**	**13**	**22,996**	**23,062**

2016	At fair value through profit or loss: Derivatives designated as fair value hedging instruments £m	At fair value through profit or loss: Held for trading £m	At fair value through profit or loss: Designated upon initial recognition £m	At fair value through Other Comprehensive income (OCI): Available for sale £m	At fair value through Other Comprehensive income (OCI): Cash flow hedge derivatives £m	Held at amortised cost £m	Total £m
Financial assets							
Cash and balances with central banks	-	-	-	-	-	1,172	1,172
Items in the course of collection from other banks	-	-	-	-	-	131	131
Derivative financial instruments	6	23	-	-	26	-	55
Loans and advances to banks	-	-	63	-	-	3,158	3,221
Available for sale financial assets	-	-	-	1,140	-	-	1,140
Loans and advances to customers	-	-	-	-	-	20,043	20,043
Total financial assets	6	23	63	1,140	26	24,504	25,762
Financial liabilities							
Deposits from banks	-	-	-	-	-	2,675	2,675
Customer accounts	-	-	63	-	-	19,541	19,604
Items in the course of transmission to other banks	-	-	-	-	-	85	85
Derivative financial instruments	75	20	-	-	7	-	102
Subordinated liabilities	-	-	-	-	-	335	335
Total financial liabilities	75	20	63	-	7	22,636	22,801

x 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.

	2017		2016	
	Fair values £m	**Contractual amount due on maturity £m**	Fair values £m	Contractual amount due on maturity £m
Customer accounts	1	1	63	59

y 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)[1]	3,000	3,000	2,886	2,886

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.

[1] *For the purposes of this disclosure, associated liabilities include liabilities issued by Bowbell, held by the Bank.*

z Fair value of assets and liabilities

	2017				2016			
	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets held at fair value								
Derivative financial instruments	-	27	-	27	-	55	-	55
Loans and advances to banks	-	1	-	1	-	63	-	63
Available for sale financial assets	1,008	-	-	1,008	1,140	-	-	1,140
Non-financial assets held at fair value								
Property held at fair value	-	-	23	23	-	-	7	7
Total assets held at fair value	**1,008**	**28**	**23**	**1,059**	**1,140**	**118**	**7**	**1,265**
As a % of fair value assets	**95%**	**3%**	**2%**	**100%**	**90%**	**9%**	**1%**	**100%**
Financial liabilities held at fair value								
Customer accounts	-	1	-	1	-	63	-	63
Derivative financial instruments	-	65	-	65	-	102	-	102
Total financial liabilities held at fair value	**-**	**66**	**-**	**66**	**-**	**165**	**-**	**165**
As a % of fair value liabilities	**-**	**100%**	**-**	**100%**	**-**	**100%**	**-**	**100%**

	2017				2016			
	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Fair value of financial assets held at amortised cost								
Loans and advances to banks	-	2,640	-	2,640	-	3,201	-	3,201
Loans and advances to customers	-	-	20,325	20,325	-	-	20,065	20,065
Total	**-**	**2,640**	**20,325**	**22,965**	**-**	**3,201**	**20,065**	**23,266**
Fair value of financial liabilities held at amortised cost								
Deposits from banks	-	3,569	-	3,569	-	2,698	-	2,698
Customer accounts	-	19,055	-	19,055	-	19,589	-	19,589
Subordinated liabilities	-	301	-	301	-	351	-	351
Total	-	**22,925**	**-**	**22,925**	**-**	**22,638**	**-**	**22,638**

Movements in level 3 assets

Property held at fair value	**2017 £m**	2016 £m
At 1 January	7	7
Additions	15	-
Revaluation of property	1	-
At 31 December	**23**	**7**

			Fair Value		Range	
Level 3 assets	**Valuation technique**	**Unobservable input**	**2017 £m**	2016 £m	**2017 %**	2016 %
Property held at fair value	Market comparable property transactions	Property valuation assumptions	23	7	Third party pricing	Third party pricing

z Fair value of assets and liabilities (continued)

	2017 Carrying amount £m	2017 Fair values £m	2016 Carrying amount £m	2016 Fair values £m
Financial Assets				
Loans and advances to banks	2,625	2,641	3,221	3,264
Loans and advances to customers	20,289	20,325	20,043	20,065
Financial Liabilities				
Deposits from banks	3,554	3,569	2,675	2,698
Customer accounts	19,045	19,056	19,604	19,652
Subordinated liabilities	290	301	335	351

The carrying amount and the fair value of the Group's financial assets and liabilities which are carried at amortised cost are set out in the table. Items where the carrying amount is a reasonable approximation of fair value are not included, as permitted by IFRS 7.

aa Related party transactions

	2017 Parent[1] £m	2017 Joint venture £m	2017 Total £m	2016 Parent[1] £m	2016 Joint venture £m	2016 Total £m
Income statement						
Interest income	3	-	3	23	-	23
Interest expense	(36)	-	(36)	(49)	-	(49)
Fees and commission expense	(8)	-	(8)	(7)	-	(7)
Net trading expense	9	-	9	(18)	-	(18)
Other operating income	-	34	34	-	35	35
Operating expenses paid for services provided[2]	(216)	-	(216)	(222)	-	(222)
Total income / (expense)	**(248)**	**34**	**(214)**	**(273)**	**35**	**(238)**
Assets						
Loans and advances to banks	1,383	-	1,383	2,027	-	2,027
Loans and advances to customers	6	-	6	6	-	6
Other assets	1	-	1	3	-	3
Derivatives	20	-	20	50	-	50
Total assets	**1,410**	**-**	**1,410**	**2,086**	**-**	**2,086**
Liabilities						
Deposits from banks	1,982	-	1,982	1,896	-	1,896
Customer accounts	8	-	8	7	-	7
Other liabilities	2	-	2	8	-	8
Derivatives	63	-	63	89	-	89
Subordinated liabilities	290	-	290	335	-	335
Total liabilities	**2,345**	**-**	**2,345**	**2,335**	**-**	**2,335**
Net exposure	**(935)**	**-**	**(935)**	**(249)**	**-**	**(249)**

Details of transactions with key management personnel are set out in note 36 of the consolidated financial statements.

[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 £52,131 (year ended 31 December 2016: £48,090) to Archie Kane, Governor and Non-executive Director of the Parent who was appointed as consultant advisor to the Group in June 2012.

ab Post balance sheet events

There are no post balance sheet events that require disclosure in the financial statements.

ac Approval of financial statements

The Board of Directors approved the financial statements on 6 March 2018.

Other Information

Principal business units and addresses

Bank of Ireland (UK) plc
Bow Bells House, 1 Bread Street, London EC4M 9BE
Tel: +44 207 236 2000
Website: www.bankofirelanduk.com

Bank of Ireland Great Britain Consumer Banking
Mortgages, Credit Cards, Personal Loans
PO Box 27, One Temple Quay, Bristol BS99 7AX
Tel: + 44 117 979 2222 and + 44 117 909 0900
Fax: + 44 117 929 3787

Bank of Ireland Great Britain Business Banking
Bow Bells House, 1 Bread Street, London EC4M 9BE
Tel: +44 207 236 2000

Bank of Ireland Northern Ireland Business Banking
1 Donegall Square South, Belfast, BT1 5LR
Tel: +44 28 9043 3000, Fax: +44 28 9043 3010

First Rate Exchange Services Limited
Falcon House, 115-123 Staines Road, Hounslow, TW3 3LL
Tel: + 44 208 577 9393, Fax: + 44 208 814 6685
Website: www.firstrate.co.uk
Managing Director: Gordon Gourlay

NIIB Group Limited (trading as Northridge Finance)
1 Donegall Square South, Belfast BT1 5LR
Tel: + 44 844 892 1848

Marshall Leasing Limited
Bridge House, Orchard Lane, Huntingdon, Cambridgeshire, PE29 3QT
Tel: + 44 148 041 4541, Fax: +44 148 045 1786

Pillar 3 disclosures

The Group's Pillar 3 document for the year ended 31 December 2017 can be accessed on the Group's website: www.bankofirelanduk.com. The Group's obligations under Article 89 of the CRD IV have been met by consolidation of Group data in the Parent's country by country reporting which is published on the Bank of Ireland Group website www.bankofireland.com.

Abbreviations

ALCo	Asset and Liability Committee
AML	Anti Money Laundering
ATM	Automatic Teller Machine
BoI	Bank of Ireland
bps	Basis points
BRC	Board Risk Committee
Brexit	The outcome of the UK referendum to leave the EU
BTL	Buy To Let
CCO	Chief Credit Officer
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CGU	Cash Generating Unit
CMA	Competition and Markets Authority
COO	Chief Operating Officer
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
EBA	European Banking Authority
ECL	Expected Credit Loss
EIR	Effective Interest Rate
EOCF	Executive Oversight Complaints Forum
ERC	Executive Risk Committee
EU	European Union
FCA	Financial Conduct Authority
FDI	Foreign Direct Investment
FLI	Forward Looking Information
FPC	Financial Policy Committee
FRES	First Rate Exchange Services Limited
FRESH	First Rate Exchange Services Holdings Limited
FSCS	Financial Services Compensation Scheme
GBP	ISO 4217 currency code for Pound Sterling
GCR	Group Credit Review
GIA	Group Internal Audit
GRPC	Group Risk Policy Committee
IAR	Individual Accountability Regime
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IBNR	Incurred but not Reported
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
IFRS IC	IFRS Interpretations Committee
ILAAP	Individual Liquidity Adequacy Assessment Process
ILTR	Indexed Long Term Repo
IRRBB	Interest Rate Risk in the Banking Book
ISDA	International Swaps and Derivatives Association
IT	Information Technology
KMP	Key Management Personnel
KPI	Key Performance Indicator
L&D	Land & Development
LCR	Liquidity Coverage Ratio
LGD	Loss Given Default
LIBOR	London Interbank Offered Rate
LLP	Limited Liability Partnership
LTD	Limited
LTV	Loan to Value
MLL	Marshall Leasing Limited
MRR	Monthly Risk Report
NSFR	Net Stable Funding Ratio
OCI	Other Comprehensive Income
ONS	Office for National Statistics
ORMF	Operational Risk Management Framework
PD	Probability of Default
PRA	Prudential Regulation Authority
PSAGC	Product & Services Approvals & Governance Committee
PTM	Personal Touch Mortgage
PwC	PricewaterhouseCoopers LLP
RAG	Red, Amber, Green
RAROC	Risk Adjusted Return on Capital
RAS	Risk Appetite Statement
RIR	Risk Improvement Roadmap
RMF	Risk Management Framework
ROE	Return on Equity
R&ORC	Regulatory and Operational Risk Committee
R UK&GMF	Retail UK and Group Manufacturing Forum
RWA	Risk Weighted Assets
SFT	Securities Financing Transaction
SME	Small / Medium Enterprises
SMMT	Society of Motor Manufacturers and Traders
SSM	Single Supervisory Mechanism
TFS	Term Funding Scheme
£m	Million
£bn	Billion
£'000	Thousands

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