Royal Bank of Scotland

Annual Report and Accounts 2015

Annual Report and Accounts

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Board of directors and secretary

Chairman
Howard Davies
Nominations (Chairman)

Executive directors
Ross McEwan
Ewen Stevenson

Independent non-executive directors

Sandy Crombie
Senior Independent Director
Remuneration (Chairman), Audit, Nominations

Alison Davis
Nominations, Remuneration, Sustainability

Morten Friis
Audit, Risk

Robert Gillespie
Nominations, Remuneration, Risk, Sustainability

Penny Hughes
Sustainability (Chairman), Risk

Brendan Nelson
Audit (Chairman), Nominations, Risk

Baroness Noakes
Risk (Chairman), Audit

Mike Rogers
Sustainability

Chief Governance Officer and Board Counsel
Aileen Taylor

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The Royal Bank of Scotland plc
Registered in Scotland No. SC90312

Audit	member of the Group Audit Committee
Nominations	member of the Group Nominations and Governance Committee
Remuneration	member of the Group Performance and Remuneration Committee
Risk	member of the Board Risk Committee
Sustainability	member of the Sustainable Banking Committee

Presentation of information

In the Report and Accounts, and unless specified otherwise, the terms 'the Royal Bank', 'RBS plc' or 'the Bank' mean The Royal Bank of Scotland plc, the 'Group' means the Bank and its subsidiaries, 'RBSG' or the 'holding company' mean The Royal Bank of Scotland Group plc', 'RBS Group' means the holding company and its subsidiaries, and 'NatWest' means National Westminster Bank Plc.

The Bank publishes its financial statements in pounds sterling ('£' or 'sterling'). The abbreviations '£m' and '£bn' represent millions and thousands of millions of pounds sterling, respectively, and references to 'pence' represent pence in the United Kingdom ('UK'). Reference to 'dollars' or '$' are to United States of America ('US') dollars. The abbreviations '$m' and '$bn' represent millions and thousands of millions of dollars, respectively, and references to 'cents' represent cents in the US. The abbreviation '€' represents the 'euro', the European single currency, and the abbreviations '€m' and '€bn' represent millions and thousands of millions of euros, respectively.

Business structure

The RBS Group continues to deliver on its plan to build a strong, simple and fair bank for both customers and shareholders. To support this and reflect the progress made the previously reported operating segments have been realigned as follows:

Personal & Business Banking (PBB) comprises two reportable segments, UK Personal & Business Banking (UK PBB) and Ulster Bank RoI. UK PBB serves individuals and mass affluent customers in the UK together with small businesses (generally up to £2 million turnover). UK PBB includes Ulster Bank customers in Northern Ireland. Ulster Bank RoI serves individuals and businesses in the Republic of Ireland (RoI).

Commercial & Private Banking (CPB) comprises three reportable segments, Commercial Banking, Private Banking and RBS International (RBSI). Commercial Banking serves commercial and corporate customers in the UK and Western Europe. Private Banking serves UK connected high net worth individuals and RBSI serves retail, commercial, corporate and financial institution customers in Jersey, Guernsey, Isle of Man and Gibraltar.

Corporate & Institutional Banking (CIB) serves UK and Western European corporate customers, and global financial institutions, supported by trading and distribution platforms in the UK, US and Singapore.

Capital Resolution includes CIB Capital Resolution and the remainder of RBS Capital Resolution (RCR).

Williams & Glyn (W&G) comprises the RBS England and Wales branch-based businesses, along with certain small and medium enterprises (SME) and corporate activities across the UK. During the period presented W&G has not operated as a separate legal entity. The perimeter of the segment currently reported does not include certain portfolios that are ultimately intended to be divested as part of W&G, for example, certain NatWest branches in Scotland.

Central items & other includes corporate functions, such as treasury, finance, risk management, compliance, legal, communications and human resources. Central functions manages RBS Group capital resources and RBS Group-wide regulatory projects and provides services to the reportable segments. Balances in relation to Citizens and the international private banking business that is included in disposal groups are included in Central items in the relevant periods.

Reporting changes

In line with RBS Group's strategy to be a simpler bank the following reporting changes have been implemented in relation to the presentation of the Group results:

The following items previously reported separately after operating profit/(loss) are now being reported within operating profit/(loss).

- Own credit adjustments;
- Gain/(loss) on redemption of own debt;
- Write-down of goodwill; and
- Strategic disposals.

Own credit adjustments are included within segmental results in CIB, Capital Resolution and Central items (Treasury) in line with where the related liabilities are recorded. The non-statutory segmental results will continue to show these items and restructuring costs and litigation and conduct costs as separate line items within the relevant caption of the income statement where significant.

Citizens

Citizens was classified as a discontinued operation and as a disposal group on 31 December 2014 and its assets and liabilities from that date to 3 August 2015 have been aggregated and presented as separate lines in accordance with IFRS 5. On 3 August 2015, the Group's interest in Citizens fell to 20.9% and consequently it is treated as an associate held for sale thereafter. On 30 October 2015, the Group sold all of its remaining shareholding in Citizens. Citizens is no longer treated as a reportable segment.

Comparatives have been restated accordingly for the changes outlined above.

Pensions accounting policy

As set out in 'Accounting policies' on page 148, the Group has revised its accounting policy for determining whether or not it has an unconditional right to a refund of surpluses in its employee pension funds. The change has been applied retrospectively and comparatives restated.

Top and emerging risks

Top and emerging risks

RBS Group employs a robust process for identifying and managing its top and emerging risks. Top risks are defined as scenarios that, while unlikely, may materialise, and which, if they did, would have a significant negative impact, such that RBS Group as a whole, or a particular business, could potentially fail to meet one or more of its strategic objectives. A number of scenarios attracted particular attention in 2015:

Macro-economic and other external risks

Risks related to the wider economy:

Like most other businesses, RBS Group remains vulnerable to changes in the external economic environment. Among potential scenarios considered, the following could have a material negative impact: a UK recession including large house price falls; vulnerabilities in emerging market economies, including China, resulting in contagion in RBS Group's core markets; global deflation; volatility in international markets linked to advanced economy interest rate increases or decreases; a resumption of the eurozone crisis, including a worsening of the situation in Greece; and major geopolitical instability. To mitigate these risks, RBS Group has strengthened its capital, liquidity and leverage positions. A number of higher-risk portfolios have been exited or reduced. Stress testing is used extensively to inform strategic planning and risk mitigation relating to these risks.

Risks related to the UK referendum on EU membership:

The referendum on the UK's membership of the EU during this parliament increases economic and operational uncertainty. The result may also give rise to further political uncertainty regarding Scottish independence. RBS Group actively monitors, and considers responses to, varying EU referendum outcomes to ensure that it is well prepared for all eventualities.

Risks related to the competitive environment:

RBS Group's target markets are highly competitive, which poses challenges in terms of achieving some strategic objectives. Moreover, changes in technology, customer behaviour and business models in these markets have accelerated. RBS Group monitors the competitive environment and associated technological and customer developments as part of its strategy development and makes adjustments as appropriate.

An increase in obligations to support pension schemes:

If economic growth stagnates, and interest rates remain low, the value of pension scheme assets may not be adequate to fund pension scheme liabilities.

The deficit in RBS Group pension schemes as determined by the most recent triennial valuations has increased, requiring RBS Group to increase its current and future cash contributions to the schemes. An acceleration of certain previously committed pension contributions in Q1 2016 will reduce this risk. Depending on the economic and monetary conditions and longevity of scheme members prevailing at that time, the deficit may increase at subsequent valuations.

Regulatory and legal risks

The impacts of past business conduct:

Future conduct and litigation charges could be substantial. RBS Group is involved in ongoing class action litigation, securitisation and mortgage-backed securities related litigation, investigations into foreign exchange trading and rate- setting activities, continuing LIBOR-related litigation and investigations, investigations into the treatment of small and medium- sized business customers in financial difficulty, anti-money laundering, sanctions, mis-selling (including mis-selling of payment protection insurance products), and other investigations. Settlements may result in additional financial penalties, non-monetary penalties or other consequences, which may be material. More detail on these issues can be found in the Litigation, Investigations and Reviews and Risk Factors sections. To prevent future conduct from resulting in similar impacts, RBS Group has embarked on a programme to embed a strong and comprehensive risk and compliance culture.

Risks to income, costs and business models arising from regulatory requirements:

RBS Group is exposed to the risk of further increases in regulatory capital requirements as well as risks related to new regulations that could affect its business models. RBS Group considers the implications of proposed or potential regulatory activities in its strategic and financial plans.

Operational and execution risks

Increased losses arising from a failure to execute major projects successfully:

The successful execution of major projects, including the transformation plan, the restructuring of CIB, the divestment of Williams & Glyn and the embedding of a strong and pervasive organisational and risk culture, are essential to meet RBS Group's strategic objectives. The separation and eventual divestment of Williams & Glyn is a complex process and as such entails significant operational and execution risk. The Group remains committed to full divestment of Williams & Glyn by the end of 2017. These projects cover organisational structure, business strategy, information technology systems, operational processes and product offerings. RBS Group is working to implement change in line with its project plans while assessing the risks to implementation and taking steps to mitigate those risks where possible.

Impact of cyber attacks:

Cyber attacks are increasing in frequency and severity across the industry. RBS Group has participated in industry-wide cyber attack simulations in order to help test and develop defence planning. To mitigate the risks, a large-scale programme to improve user access controls is in progress, along with a number of other actions, including a reduction in the number of external websites, enhancement of anti-virus protections, and the implementation of a staff education programme on information protection.

Top and emerging risks

Inability to recruit or retain suitable staff:
RBS Group is undergoing significant organisational change, the result of a need to implement new business strategies and respond to a changing external environment. The pace of change, coupled with the associated uncertainty, may cause experienced staff to leave and prospective staff not to join. Although these risks concern all customer businesses, they particularly affect CIB. RBS Group has communicated expected changes in its organisational structure to members of staff, implementing plans aimed at minimising unexpected staff losses. It is also working to implement an enhanced recruitment strategy.

Failure of information technology systems:
RBS Group's information technology systems may be subject to failure. As such systems are complex, recovering from failure is challenging. To mitigate these risks, a major investment programme has significantly improved the resilience of the systems and more benefits are expected. Back-up system sustainability has improved, and a 'shadow bank' system, to provide basic services, if needed, has been created.

Full risk factors are discussed on pages 268 to 293.

Financial review

Financial summary

Summary consolidated income statement for the year ended 31 December 2015

	2015 £m	2014 £m
Net interest income	8,408	8,866
Fees and commissions receivable	3,692	4,320
Fees and commissions payable	(805)	(842)
Income from trading activities	954	1,190
(Loss)/gain on redemption of own debt	(263)	6
Other operating income	165	1,078
Non-interest income	3,743	5,752
Total income	12,151	14,618
Operating expenses	(16,141)	(13,552)
(Loss)/profit before impairment releases	(3,990)	1,066
Impairment releases	837	1,337
Operating (loss)/profit before tax	(3,153)	2,403
Tax credit/(charge)	29	(2,033)
(Loss)/profit from continuing operations	(3,124)	370
Profit/(loss) from discontinued operations, net of tax	1,538	(3,486)
Loss for the year	(1,586)	(3,116)
Non-controlling interests	(320)	(57)
Preference dividends	(44)	(61)
Loss attributable to ordinary shareholders	(1,950)	(3,234)

2015 compared with 2014

The Group reports a loss for the year of £1,586 million compared with a loss of £3,116 million in 2014. This included profit from discontinued operations of £1,538 million, compared with a loss of £3,486 million in 2014. Operating expenses increased by £2,589 million to £16,141 million compared with £13,552 million in 2014, primarily due to increased litigation and conduct costs and restructuring costs and a charge for goodwill impairment of £498 million attributed to Private Banking. Loss on redemption of own debt was £263 million compared with a gain of £6 million in 2014.

Operating (loss)/profit before tax

Operating loss before tax was £3,153 million compared with a profit of £2,403 million in 2014. The decrease reflects lower income of £12,151 million, compared with £14,618 million in 2014, primarily due to income attrition and disposal losses in the Capital Resolution business. Net impairment releases were lower at £837 million, compared with £1,337 million in 2014. Operating expenses were £16,141 million (2014 - £13,552 million) and included higher litigation and conduct costs of £3,507 million (2014 - £2,202 million) primarily relating to additional provisions for mortgage backed securities litigation in the US (£2.1 billion) and PPI costs of £600 million. Restructuring costs were £2,903 million (2014 - £1,154 million) as the transformation of the Group accelerated, particularly in CIB.

Net interest income

Net interest income decreased by £458 million, or 5%, to £8,408 million, driven principally by a 52% reduction in Capital Resolution, down £468 million to £440 million, in line with the planned shrinkage of the balance sheet. UK PBB net interest income was £4,263 million compared with £4,277 million in 2014 as competitive front book margin pressures impacted. Ulster Bank RoI net interest income fell by £102 million, 22%, to £365 million primarily due to the weakening of the euro relative to sterling and reduced income on free funds.

Financial review

Non-interest income

Non-interest income decreased by £2,009 million, 35%, to £3,743 million compared with £5,752 million in 2014. Own credit adjustments represented a gain of £329 million compared with a charge of £128 million in 2014. Net fees and commissions decreased by £591 million, 17%, to £2,887 million mainly due the reduced scale of activity in CIB, run down of Capital Resolution and lower card interchange fees in UK PBB. Income from trading activities was down £236 million to £954 million, compared with £1,190 million in 2014 due to the reduced scale and resources in CIB and the continued planned reduction of the Capital Resolution business.

A loss of £263 million was recognised on the redemption of own debt, from a liability management exercise to repurchase certain US dollar, sterling and euro senior debt securities, compared with a gain of £6 million in 2014. Other operating income reduced by £913 million, or 85%, to £165 million, principally due to the reduced scale of CIB together with the run down of Capital Resolution and the impact of disposal losses.

Operating expenses

Operating expenses increased by £2,589 million, or 19%, to £16,141 million from £13,552 million in 2014 and included a charge for goodwill impairment of £498 million attributed to Private Banking (2014 - £130 million in Capital Resolution). Operating expenses, excluding restructuring costs and litigation and conduct costs, decreased by £465 million, or 5%, to £9,731 million (2014 - £10,196 million) mainly reflecting the benefits of cost savings initiatives.

Litigation and conduct costs were £3,507 million compared with £2,202 million in 2014, primarily relating to mortgage backed securities litigation in the US of £2.1 billion. Other charges in 2015 include: provisions for foreign exchange investigations in the US, £334 million, customer redress provisions primarily relating to PPI of £600 million, Interest Rate Hedging Products redress of £81 million and other litigation and conduct provisions of £392 million including provisions relating to packaged accounts and investment products.

Restructuring costs increased by £1,749 million to £2,903 million, compared with £1,154 million in 2014, as the transformation of the Group accelerated, particularly re-engineering the CIB business.

Impairment releases/(losses)

Net impairment releases were £837 million in 2015 compared with net impairment releases of £1,337 million in the prior year. Capital Resolution recorded net releases of £781 million, compared with £1,293 million in 2014, with disposal activity continuing. Ulster Bank RoI recorded net impairment releases of £141 million, down from £306 million in 2014, as economic conditions in Ireland continue to improve. UK PBB recorded a release of £7 million compared with a loss of £154 million, due to lower debt flows and increased releases and recoveries. Net impairment releases were also reported in CIB, although at more modest levels.

Discontinued operations

Profit from discontinued operations was £1,538 million reflecting a gain on disposal in relation to Citizens of £249 million and in respect of reserves of £1,001 million recycled to the income statement, together with a gain of £318 million attributable to non-controlling interests. In 2014, the loss from discontinued operations was £3,486 million, which reflected an accounting write down of £3,994 million in relation to Citizens.

Capital ratios

Capital ratios for RBS plc at 31 December 2015 were 16.0% (2014 - 13.1%) (Common Equity Tier 1), 17.1% (2014 - 13.9%) (Tier 1) and 25.3% (2014 - 20.9%) (Total).

Segment performance

UK Personal & Business Banking

Income statement	2015 £m	2014 £m
Net interest income	4,263	4,277
Net fees and commissions	970	1,111
Other non-interest income	28	61
Non-interest income	998	1,172
Total income	5,261	5,449
Direct expenses		
- staff costs	(801)	(824)
- other costs	(256)	(330)
Indirect expenses	(1,492)	(1,479)
Restructuring costs		
- direct	(38)	(10)
- indirect	(132)	(83)
Litigation and conduct costs	(921)	(906)
Operating expenses	(3,640)	(3,632)
Operating profit before impairment losses	1,621	1,817
Impairment releases/(losses)	7	(154)
Operating profit	1,628	1,663
Operating expenses - adjusted (1)	(2,549)	(2,633)
Operating profit - adjusted (1)	2,719	2,662

Balance sheet	£bn	£bn
Loans and advances to customers (gross)		
- personal advances	6.0	6.5
- mortgages	104.8	95.5
- business	5.3	5.9
- cards	4.1	4.7
- other	1.4	1.5
Total loans and advances to customers (gross)	121.6	114.1
Loan impairment provisions	(1.8)	(2.5)
Net loans and advances to customers	119.8	111.6
Total assets	127.1	119.8
Funded assets	127.1	119.8
Total customer deposits	137.8	132.6
Assets under management (excluding deposits)	4.3	4.9

Note:
(1) Excluding restructuring costs and litigation and conduct costs

Key points

UK Personal & Business Banking (UK PBB) made signficant positive changes to the customer proposition in 2015, whilst becoming simpler and fair. We have seen a number of key customer metrics improve. Results now include Ulster Bank Northern Ireland and exclude Williams & Glyn, which is reported as a separate segment.

Delivering enhanced digital capabilities:

- In February RBS became the first UK bank to launch TouchID, enabling customers to log-in to its mobile app using only their fingerprint.
- Enabled real time registration of our mobile banking app, allowing customers to log-in immediately as they open their new current account.
- Continued to be at the forefront of technological collaboration; one of the first UK banks to launch Apple Pay whilst developing an Apple Watch app.
- Customers using the mobile app increased 27% to 3.7 million in 2015 as we continue to invest in and enhance the platform to reflect the growing customer preference for this channel.
- Launched online diary where customers can book an appointment with an advisor from the comfort of their own home.

Launched market differentiating propositions:

- UK PBB continued to invest in building deeper engagement with our customers through the launch of our new banking proposition – “Reward” whereby customers receive 3% cashback on their household bills.
- Launched the fee-free Foundation account to better support the 1.5 million unbanked individuals in the UK.
- We launched testing of small value overdrafts to c.1 million customers, specifically to help customers avoid unexpected fees.
- Launched an online mortgage application tracker to improve customer experience.
- Launched an innovative new home insurance product offering customers a fixed premium for three years, which we believe is a positive departure from industry practice.
- Launched Royal National Institute of Blind People (RNIB) approved cards, becoming the first UK bank product to achieve RNIB accreditation.

Helping UK homebuyers:

- In 2015 the business made a concerted investment in its mortgage business, increasing mortgage advisors by 21% from 803 to 974 (excluding Ulster Bank NI). This contributed to a strong year for mortgage lending with net balances increasing by £9.3 billion to £104.8 billion.
- One of the first UK banks to offer the UK Government-led Help to Buy: ISA as we continue to help first time buyers. NatWest and Ulster Bank customers are offered a variable rate of 2% AER and can save up to £1,200 in the first month.

Operational investment continued apace:

- New onboarding system for Business Banking was completed in November 2015. It has reduced the average account opening time by 50% from 15 days to 7 days and we are onboarding c. 500 new customers every day.
- We continue to invest and improve our branch network to meet the demands and enrich the experience of our customers. During 2015, 322 branches received an upgrade via our Branch Transformation programme.
- We replaced 922 ATMs during the year.
- Time to open a new current account reduced by 50%, allowing frontline staff more time to have great customer conversations.

Investing in our people:

- We continue on our journey to enhance the capability of our people. During the year, we have made significant further investment in training our leaders, in rolling out skills-based pay in our telephony centres and in introducing the new Personal Banker role in branches, enabling more of our staff to fulfil customer needs.
- We also announced the ending of incentives for our frontline staff from January 2016, which has been positively received and will ensure our staff are focused on what is best for the customer.

2015 compared with 2014

UK PBB recorded an operating profit of £1,628 million in 2015, a reduction of 2% or £35 million from 2014. This was primarily driven by lower non-interest income combined with increased restructuring costs and litigation and conduct costs. This was partially offset by a small net impairment release compared with a prior year charge. Adjusted operating profit of £2,719 million increased by 2% or £57 million from 2014.

Total income was £5,261 million, a reduction of 3% from £5,449 million. Net interest income was relatively flat at £4,263 million. Continued margin pressure in the mortgage market as customers move to lower margin fixed rate products together with higher internal funding costs was offset by the improved deposit margins.

Non-interest income was £998 million, a reduction of 15% compared with the prior year as interchange fees on credit and debit cards declined £59 million, combined with reduced advice income.

Operating expenses were £3,640 million, remaining broadly stable against 2014. Litigation and conduct costs increased 2% due to customer redress provisions, primarily relating to PPI, to £921 million, whilst higher restructuring costs were up £77 million, to £170 million. This was principally offset by a reduction in staff and other costs. Adjusted operating expenses totalled £2,549 million, 3% lower than 2014.

Net impairment releases totalled £7 million, compared with a net charge of £154 million in 2014, driven by decreased charges from bad debt flows and benefit of provision releases and recoveries.

2015 was a strong year for the mortgage business with applications increasing 48% from £21.7 billion to £32.0 billion as gross new lending rose 29% to £23 billion. Market share of new mortgages was 10.5% versus a stock share of 8.2%. This led to net mortgage balances growing by £9.3 billion or 10% to £104.8 billion.

Customer deposit balances increased £5.2 billion to £137.8 billion due to growth in personal savings, current accounts and business banking.

Ulster Bank RoI

Income statement	2015 €m	2014 €m	2015 £m	2014 £m
Net interest income	503	579	365	467
Net fees and commissions	116	116	85	93
Other non-interest income	139	54	100	44
Non-interest income	255	170	185	137
Total income	758	749	550	604
Direct expenses				
- staff costs	(220)	(203)	(160)	(164)
- other costs	(116)	(104)	(85)	(83)
Indirect expenses	(188)	(163)	(136)	(131)
Restructuring costs				
- direct	(17)	10	(12)	8
- indirect	(4)	(21)	(3)	(17)
Litigation and conduct costs	18	24	13	19
Operating expenses	(527)	(457)	(383)	(368)
Operating profit before impairment losses	231	292	167	236
Impairment releases	194	380	141	306
Operating profit	425	672	308	542
Operating expenses - adjusted (1)	(524)	(470)	(381)	(378)
Operating profit - adjusted (1)	428	659	310	532

Balance sheet	€bn	€bn	£bn	£bn
Loans and advances to customers (gross)				
Mortgages	18.8	19.6	13.8	15.3
Commercial real estate				
- investment	0.9	1.3	0.7	1.0
- development	0.3	0.3	0.2	0.3
Other corporate	4.8	4.5	3.5	3.4
Other lending	0.5	0.7	0.4	0.5
Total loans and advances to customers (gross)	25.3	26.4	18.6	20.5
Loan impairment provisions	(2.6)	(3.1)	(1.9)	(2.4)
Net loans and advances to customers	22.7	23.3	16.7	18.1
Total assets	29.0	28.9	21.3	22.5
Funded assets	28.8	28.7	21.2	22.4
Customer deposits	17.8	18.9	13.1	14.7

Note:
(1) Excluding restructuring costs and litigation and conduct costs.

Financial review

Key points

Following the strategic review of Ulster Bank Limited in 2014, it was confirmed that the Northern Ireland and Republic of Ireland businesses were to be separated. The change of management controls and governance was completed in October 2015 with the Northern Irish business included in UK Personal & Business Banking (UK PBB) and the reportable segment of Ulster Bank RoI now comprising the core Republic of Ireland business only.

Ulster Bank RoI has continued to strengthen its customer offering and service capability in 2015 as it made it simpler for customers to do business. The year has also seen stronger new lending volumes, buoyed by the improving economic conditions:

- Further investment in the mortgage business through the launch of the "mortgage you can live with" campaign which offers a range of new product options to both new and existing customers combined with a re-entry to the mortgage broker market and the introduction of a team of mobile mortgage managers. Gross new mortgage lending increased 53% to £0.5 billion in 2015.
- Delivered new propositions for commercial customer lending across several sectors, including food and drink, agriculture, asset finance and international business. Gross new lending to commercial customers increased by 65% to £1.1 billion from 2014.
- Made it easier for our customers to bank with us. The bank's current account proposition was re-launched in October and a partnership with 'An Post' provides customers with 1,140 new points of presence.

2015 compared with 2014

A significant weakening of the euro relative to sterling during 2015 had a material impact on Ulster Bank RoI's financial comparison with 2014 and the income trend in particular.

Ulster Bank RoI recorded an operating profit of £308 million compared with an operating profit of £542 million in 2014, the decline was primarily due to considerably lower net impairment releases in 2015. Adjusted operating profit was £310 million, a decrease of £222 million from 2014.

Total income was £550 million, a decrease of 9% from the prior year reflecting the weakening of the euro during 2015. Excluding the impact of the euro exchange rate movement, total income increased 1% due to a continued improvement in deposit pricing in line with market trends, combined with non-recurring benefits, including a gain on the sale of a buy-to-let portfolio of £12 million and the closure of a foreign exchange exposure of £24 million. These benefits were largely offset by reduced income on free funds.

Operating expenses increased by 4% from £368 million to £383 million, reflecting an increase in pension servicing costs, totalling £22 million, partially offset by the benefit of a weakening euro. Cost savings delivered through a further reduction in both employee numbers and the property footprint were somewhat offset by further investment in the business and operational infrastructure.

Net impairment releases reduced by £165 million to £141 million, and although at lower levels, continued to reflect the improving economic conditions and the benefits of proactive debt management.

Gross new mortgage lending increased 53% to £0.5 billion whilst gross new lending to commercial customers increased 65% to £1.1 billion. Strong new lending volumes across the business in 2015 were offset by high levels of customer repayments and the sale of a £0.3 billion buy-to-let mortgage portfolio. Net loans and advances to customers decreased £1.4 billion to £16.7 billion, £1 billion of which related to exchange rate movements. The low yielding tracker mortgage portfolio balances reduced from £10.6 billion in 2014 to £9.2 billion, but continues to make up a significant part of the overall mortgage book.

Commercial Banking

Income statement	2015 £m	2014 £m
Net interest income	2,195	2,130
Net fees and commissions	984	983
Other non-interest income	273	348
Non-interest income	1,257	1,331
Total income	3,452	3,461
Direct expenses		
- staff costs	(483)	(496)
- other costs	(96)	(104)
- operating lease costs	(141)	(141)
Indirect expenses	(699)	(656)
Restructuring costs		
- direct	(52)	(40)
- indirect	(14)	(58)
Litigation and conduct costs	(51)	(112)
Operating expenses	(1,536)	(1,607)
Operating profit before impairment losses	1,916	1,854
Impairment losses	(69)	(85)
Operating profit	1,847	1,769
Operating expenses - adjusted (1)	(1,419)	(1,397)
Operating profit - adjusted (1)	1,964	1,979

Balance sheet	2015 £bn	2014 £bn
Loans and advances to customers (gross)		
- Commercial real estate	16.7	16.6
- Asset and invoice finance	14.4	14.2
- Private sector services (education, health, etc)	6.7	6.8
- Banks & financial institutions	7.1	5.5
- Wholesale and retail trade repairs	7.5	6.8
- Hotels and restaurants	3.3	3.3
- Manufacturing	5.3	3.9
- Construction	2.1	2.0
- Other	28.9	26.7
Total loans and advances to customers (gross)	92.0	85.8
Loan impairment provisions	(0.7)	(0.9)
Net loans and advances to customers	91.3	84.9
Total assets	97.0	90.7
Funded assets	97.0	90.7
Customer deposits (excluding deposits)	88.9	84.9

Note:
(1) Excluding restructuring costs and litigation and conduct costs.

Key points

Commercial Banking made progress towards improving customer experience by becoming easier and simpler to do business with through operational investment and process simplifications. Continued enhancements within the business contributed to commercial lending growth in 2015.

In the course of the year Commercial Banking:

- Opened four Entrepreneur Hubs across the UK, increasing our involvement to seven, enabling entrepreneurs and small businesses to access free office space, mentoring and financial support, with a further five hubs to be opened in 2016.
- Rolled out a new on-boarding and account opening system across England and Wales which has delivered a reduction in customer paper work and a reduction in account opening times of approximately 30%.
- Launched a lending pilot to upgrade and simplify end-to-end processes with a focus on streamlining our product, pricing and governance operations.
- Issued 12,500 statements of appetite letters to customers, offering up to £8 billion of new borrowing facilities as part of our continued support of UK business.
- Supported AB Inbev's acquisition of SABMiller, the fifth largest corporate takeover ever and largest in the UK.
- Awarded Residential Funder of the Year, providing finance for c.20k homes to be built in 2015.
- Our Commercial Relationship Bankers are undertaking intensive training and development, accredited by the Chartered Bankers Institute, with over 5,000 participants.
- Grew net new lending by £3.6 billion excluding the impact of the transferred businesses from CIB and strategic run-off decisions.
- Proactive capital management with £2.2 billion of lower performing assets run-off in 2015.

2015 compared with 2014

Comparisons with prior periods are affected by a number of internal business transfers. In line with changes to the business model, the UK and Western European corporate loan portfolios transferred to Commercial Banking on 1 May 2015 and 1 October 2015 respectively. The prior period financials were adjusted for the UK Transaction Services business transfer and do not affect comparisons. The results exclude RBS International which is reported as a separate segment for the first time.

Commercial Banking recorded an operating profit of £1,847 million, broadly in line with the prior year. Adjusted operating profit was £1,964 million, a decrease of £15 million from 2014 due to a marginal fall in income reflecting margin pressure.

Total income was £3,452 million, compared with £3,461 million in 2014. Net interest income was £2,195 million, a 3% increase from 2014, driven largely by higher asset and deposit volumes. Non-interest income fell by 6% to £1,257 million driven by a loss of £34 million from the sale of non-strategic asset portfolios and the transfer of the commercial cards business to UK PBB in 2014.

Operating expenses totalled £1,536 million, a reduction of 4% from 2014, principally driven by tight control on discretionary costs and lower litigation and conduct costs, down 54% to £51 million, combined with restructuring costs falling 33% to £66 million. Adjusted operating expenses were £1,419 million, an increase of £22 million, primarily as a result of a higher UK bank levy charge.

Net impairment losses decreased £16 million to £69 million due to lower individual charges, offsetting lower net provision releases.

Commercial Banking recorded volume growth across segments, resulting in net loans and advances to customers increasing by £6.4 billion to £91.3 billion. This included £5.0 billion from the transferred businesses, offset by strategic run-off and sale of selected assets totalling £2.2 billion. Excluding the transferred businesses and strategic run-off and disposals, net new lending was £3.6 billion.

Customer deposits totalled £88.9 billion, an increase of £4.0 billion reflecting high levels of liquidity in the market.

The Commercial Banking run-off portfolio includes funded assets of £12.5 billion.

Private Banking

Income statement	2015 £m	2014 £m
Net interest income	410	454
Net fees and commissions	186	214
Other non-interest income	22	21
Non-interest income	208	235
Total income	618	689
Direct expenses		
- staff costs	(176)	(178)
- other costs	(35)	(38)
Indirect expenses	(224)	(202)
Restructuring costs		
- direct	(7)	(1)
- indirect	(66)	3
Litigation and conduct costs	(12)	(90)
Write down of goodwill	(498)	—
Operating expenses	(1,018)	(506)
Operating (loss)/profit before impairment (losses)/releases	(400)	183
Impairment (losses)/releases	(13)	5
Operating (loss)/profit	(413)	188
Operating expenses - adjusted (1)	(435)	(418)
Operating profit - adjusted (1)	170	276

Balance sheet	2015 £bn	2014 £bn
Loans and advances to customers (gross)		
- Personal	2.7	2.6
- Mortgages	6.5	6.1
- Other	2.0	2.3
Total loans and advances to customers (gross)	11.2	11.0
Loan impairment provisions	—	—
Net loans and advances to customers	11.2	11.0
Total assets	11.6	12.2
Funded assets	11.6	12.2
Assets under management	13.9	13.8
Customer deposits (excluding repos)	23.1	22.3

Note:
(1) Excluding restructuring costs and litigation and conduct costs and write down of goodwill.

Key points

Private Banking is being repositioned to focus on its UK connected customers and implement growth initiatives to create long term sustainable returns. The business has moved forward with simplifying its operating model and continued to develop new customer propositions for wealthy individuals and families. Private Banking results exclude the international private banking business given its plan for disposal.

Private Banking continued to invest in the customer proposition whilst moving toward a more focused business model:

- Strategic repositioning to focus on UK customers with the sale of the European, the Middle East and Africa tranche of the international private banking business completed in Q4 2015. The smaller Far East tranche is scheduled to complete in the first half of 2016.
- A series of customer initiatives to ensure client connectivity has resulted in a 29% increased use of digital channels, increased volumes of payments and transfers with a rise in the client satisfaction score.
- Growth in customer referrals from Personal & Business Banking and Commercial Banking has driven increased client introductions and on-boarding.
- Operational enhancements delivered in the credit application process combined with improved customer experience through improved fraud detection functionality.
- Global Private Banking Awards 2015: Coutts named best Private Bank in the UK.

2015 compared with 2014

Private Banking recorded an adjusted operating profit of £170 million, a fall of £106 million reflecting lower income and higher impairment losses. A charge for goodwill impairment of £498 million attributed to the business drove an operating loss of £413 million, compared with an operating profit of £188 million in 2014.

Total income was £618 million, a reduction of £71 million from 2014. Net interest income was £410 million, down 10% primarily due to lower net interest margin. Non-interest income totalled £208 million, a decrease of 11% driven by lower investment and transactional income as the business adjusted pricing to reflect a more competitive market.

Adjusted operating expenses were £435 million, up 4%, with reductions in the direct cost base offset by a higher UK bank levy charge. Operating expenses totalled £1,018 million, an increase of £512 million, driven by a goodwill impairment charge of £498 million, and considerably higher restructuring costs of £73 million which included a share of an asset write down related to software of £91 million, and lower litigation and conduct costs of £12 million.

Net impairment losses totalled £13 million, compared with a release of £5 million, due to higher individual and latent charges.

Despite challenging market conditions, assets under management and net loans and advances to customers were broadly stable compared with the prior year.

RBS International

Income statement	2015 £m	2014 £m
Net interest income	303	323
Net fees and commissions	40	43
Other non-interest income	24	25
Non-interest income	64	68
Total income	367	391
Direct expenses		
- staff costs	(42)	(44)
- other costs	(16)	(15)
Indirect expenses	(58)	(51)
Restructuring costs		
- direct	—	(2)
- indirect	(4)	(5)
Operating expenses	(120)	(117)
Operating profit before impairment releases	247	274
Impairment releases	—	7
Operating profit	247	281
Operating expenses - adjusted (1)	(116)	(110)
Operating profit - adjusted (1)	251	288

Balance sheet	2015 £bn	2014 £bn
Loans and advances to customers (gross)		
- Corporate	4.5	4.5
- Mortgages	2.5	2.6
- Other	0.4	0.2
Total loans and advances to customers (gross)	7.4	7.3
Loan impairment provisions	(0.1)	(0.1)
Net loans and advances to customers	7.3	7.2
Total assets	7.9	7.8
Funded assets	7.9	7.8
Customer deposits	21.3	20.8

Note:
(1) Excluding restructuring costs.

Financial review

Key points

RBS International (RBSI) operates under the CPB franchise, serving retail, commercial, corporate and financial institution customers in Jersey, Guernsey, Isle of Man and Gibraltar. RBSI is reported as a separate segment for the first time. RBSI leverages a strong multi-currency banking platform combined with a comprehensive product suite. RBSI completed a strategy review at the end of 2015 with plans to invest in and grow the business now being implemented, with particular focus on the funds and mortgage businesses.

During 2015 RBSI has enhanced its customer offering:

- Invested in the multi-currency online banking platform, a unique system to RBSI, to ensure a transformative service to further simplify customer experience.
- Continued its support for Gibraltar's largest private sector turnover company through a syndicated working capital facility.

2015 compared with 2014

RBSI reported an operating profit of £247 million, £34 million lower than 2014, largely due to lower income from deposits.

Total income decreased 6% to £367 million, mainly due to reductions in net interest income, falling £20 million to £303 million, principally reflecting lower deposit margins and lower return on free funds partly offset by higher asset volumes. Non-interest income declined £4 million to £64 million as a result of a lower CIB revenue share and lower net lending fees.

There were no impairments in 2015 compared with modest impairment releases of £7 million in the prior year.

Operating expenses remained stable at £120 million due to control in direct expenditure offset by a slightly higher UK bank levy charge.

Net loans and advances to customers increased by £0.1 billion to £7.3 billion. Customer deposit balances grew £0.5 billion to £21.3 billion.

Corporate & Institutional Banking

	2015 £m	2014 £m
Net interest income	82	117
Net fees and commissions	218	408
Income from trading activities	1,153	1,386
Other non-interest income	(51)	157
Own credit adjustments	120	(9)
Non-interest income	1,440	1,942
Total income	1,522	2,059
Direct expenses		
- staff costs	(348)	(446)
- other costs	(122)	(190)
Indirect expenses	(659)	(706)
Restructuring costs		
- direct	(44)	(13)
- indirect	(480)	(72)
Litigation and conduct costs	(378)	(832)
Operating expenses	(2,031)	(2,259)
Operating loss before impairment releases	(509)	(200)
Impairment releases	5	7
Operating loss	(504)	(193)
Total income - adjusted (1)	1,402	2,068
Operating expenses - adjusted (2)	(1,129)	(1,342)
Operating profit - adjusted (1,2)	278	733

Balance sheet	£bn	£bn
Loans and advances to customers (gross, excluding reverse repos)	16.1	26.5
Loans and advances to banks (excluding reverse repos) (3)	6.5	2.5
Reverse repos	38.6	45.9
Securities	23.7	43.7
Cash and eligible bills	11.4	16.2
Other	4.9	8.5
Total assets	213.8	281.9
Funded assets	101.2	143.3
Customer deposits (excluding repos)	5.7	11.8

Notes:
(1) Excluding own credit adjustments.
(2) Excluding restructuring costs and litigation and conduct costs.
(3) Excludes disposal groups.

Financial review

Key points

Corporate & Institutional Banking (CIB) announced its new business strategy in February 2015, separating the segment between go-forward and CIB Capital Resolution (now Capital Resolution).

The current CIB business is undergoing a multi-year transformation implementing a simpler and sustainable operating model as the business re-shapes and downsizes. The business has been shaped around three product lines: Rates, Currencies and Financing with core focus on UK and Western European corporates and global financial institutions.

2015 compared with 2014

CIB reported an operating loss of £504 million in 2015, compared with an operating loss of £193 million in 2014. This included restructuring costs of £524 million and litigation and conduct costs of £378 million. The adjusted operating profit was £278 million, compared with a profit of £733 million in 2014. The reduction was driven by lower income partially offset by the continued reduction in adjusted expenses, down £213 million, or 16%, to £1,129 million as the business continues to take costs out and move towards a more sustainable cost base.

Total income declined by £537 million, or 26%, to £1,522 million in 2015, reflecting the reduced scale and scope of the business.

Operating expenses fell by £228 million, or 10%, to £2,031 million in 2015. Adjusted operating expenses fell by £213 million or 16% to £1,129 million as the business reshaped, including a considerable reduction in headcount. Litigation and conduct costs fell by £454 million, or 55%, to £378 million, primarily relating to foreign exchange settlements in the US. This reduction was offset by an increase in restructuring costs of £439 million to £524 million, primarily relating to property and intangible asset write downs.

Funded assets fell by £42.1 billion to £101.2 billion as the business continues to work through re-shaping.

Capital Resolution

Income statement	2015 £m	2014 £m
Net interest income	440	908
Net fees and commissions	254	459
Income from trading activities	(470)	380
Other non-interest income	(7)	276
Own credit adjustments	167	(26)
Strategic disposals	(38)	—
Non-interest income	(94)	1,089
Total income	346	1,997
Direct expenses		
- staff costs	(286)	(400)
- other costs	(198)	(271)
Indirect expenses	(688)	(813)
Restructuring costs		
- direct	(361)	(78)
- indirect	(916)	(79)
Litigation and conduct costs	(2,104)	(53)
Write-down of goodwill	—	(130)
Operating expenses	(4,553)	(1,824)
Operating (loss)/profit before impairment releases	(4,207)	173
Impairment releases	781	1,293
Operating (loss)/profit	(3,426)	1,466
Total income - adjusted (1)	217	2,023
Operating expenses - adjusted (2)	(1,172)	(1,484)
Operating (loss)/profit - adjusted (1,2)	(174)	1,832

Balance sheet	£bn	£bn
Loans and advances to customers (gross, excluding reverse repos) (3)	24.5	61.4
Total assets	187.8	314.4
Funded assets	39.8	101.7
Customer deposits (excluding repos)	26.0	39.9

Notes:
(1) Excluding own credit adjustments and strategic disposals.
(2) Excluding restructuring costs, litigation and conduct costs and write-down of goodwill.
(3) Includes disposal groups.

Financial review

Key points

Capital Resolution consists of two established businesses: CIB Capital Resolution, and RBS Capital Resolution (RCR), with total funded assets of £102 billion at the start of 2015.

CIB Capital Resolution was created from non-strategic portfolios from CIB, to enable the build of a strong go-forward CIB business. Funded assets on 1 January 2015 were £88 billion, consisting of three regional portfolios (Americas, EMEA and APAC), Shipping, Markets assets, Other legacy assets including Saudi Hollandi Bank (SHB) and Global Transaction Services. There is a three stage process in place to guide the business down; starting with taking the capital out, then running down the cost base and finally managing tail risk in the longer-term.

RCR was created on 1 January 2014 and had funded assets of £13.6 billion at the start of 2015. RCR formally closed following approval from the PRA on 22 February 2016.

2015 was a year of strong progress across Capital Resolution:

CIB Capital Resolution accelerated the execution of its strategy:

- North American loan portfolios sales, removing substantially all of our North American exit portfolio;
- A partnership was formed with BNP Paribas to offer existing international customers an alternative to Global Transaction Services (GTS). Uncommitted GTS trade lending and new business has been terminated.

RCR has achieved its asset and risk reduction objectives:

- RBS Group reduced funded assets by 88% since its formation to £4.6 billion with £10.3 billion reduction in 2015. This exceeded the targeted reduction of 85%, a year ahead of schedule.

2015 compared with 2014

Capital Resolution made an operating loss of £3,426 million, including restructuring costs of £1,277 million together with litigation and conduct costs of £2,104 million primarily relating to additional provisions for mortgage-backed securities litigation in the United States. Adjusted operating expenses were reduced by £312 million, or 21% to £1,172 million, principally reflecting a fall in headcount of approximately 900. Net impairment releases of £781 million were recorded, primarily in RCR driven by the disposal strategy and favourable market and economic conditions.

Capital Resolution funded assets fell £61.9 billion to £39.8 billion.

Williams & Glyn (1)

Income statement	2015 £m	2014 £m
Net interest income	658	664
Net fees and commissions	160	170
Other non-interest income	15	18
Non-interest income	175	188
Total income	833	852
Direct expenses		
- staff costs	(209)	(196)
- other costs	(52)	(36)
Indirect expenses	(98)	(98)
Restructuring costs		
- direct	(28)	—
Operating expenses	(387)	(330)
Operating profit before impairment losses	446	522
Impairment losses	(15)	(55)
Operating profit	431	467
Operating expenses - adjusted (2)	(359)	(330)
Operating profit - adjusted (2)	459	467

Balance sheet	£bn	£bn
Loans and advances to customers (gross)		
- Retail	11.6	11.3
- Commerical	8.7	8.6
Total loans and advance to customers (gross)	20.3	19.9
Loan impairment provisions	(0.3)	(0.4)
Net loans and advances to customers	20.0	19.5
Total assets	20.1	19.6
Funded assets	20.1	19.6
Customer deposits	24.1	22.0

Notes:

(1) Does not reflect the cost base, funding, liquidity and capital profile of a standalone bank. Operating expenses include charges based on an attribution of support provided by RBS to Williams & Glyn.

(2) Excluding restructuring costs.

Key points

As part of its commitments to the European Commission (EC), RBS Group has agreed to divest part of its UK retail and commercial banking franchise. This comprises RBS branches in England and Wales and NatWest branches in Scotland, RBS Business Banking Direct and NatWest Direct Business Banking and certain mid-corporate customers across the UK. Together, this business is referred to as 'Williams & Glyn' (W&G).

W&G has c.1.6 million retail banking customers with an estimated market share of 2% in Personal Current Accounts (PCA) in the UK. The bank has c.240,000 commercial customers served, through either the retail bank or a national network of relationship managers.

W&G is in the process of being established as a fully licensed, independent, full-service retail and commercial bank, with its own operating infrastructure and platform. RBS Group continues to work towards the separation of W&G and to meeting its EC commitments to fully divest the business by the end of 2017.

Basis of presentation

This view of W&G, as it stands as a reportable segment within the RBS Group, reflects the contribution made by W&G's ongoing business to RBS Group, as distinct to the financial effects of any disposal transaction itself. These figures do not reflect the cost base, funding, liquidity and capital profile of W&G as a standalone bank and does not include certain customer portfolios which are currently reported through other reportable segments within RBS Group .

2015 compared with 2014

Operating profit was £431 million, compared with a profit of £467 million in 2014. The reduction was principally driven by lower non-interest income and restructuring costs attributed to Commercial Banking, partly offset by a lower net impairment charge. Adjusted operating profit was down £8 million to £459 million.

Total income was £833 million, compared with £852 million in 2014. Net interest income reduced £6 million to £658 million due to mortgage margin pressure from the impact of market competition on new business pricing. Non-interest income fell by 7%, primarily due to lower fee income from credit and debit cards as well as lower overdraft usage and tariffs. Operating expenses totalled £387 million, an increase of £57 million, including a restructuring charge of £28 million in Commercial Banking. Adjusted expenses increased 9% to £359 million as the business continued to stand up the central functions and operations areas resulting in an increase in staff costs of 7% or £13 million.

Net impairment losses were £15 million, lower than the £55 million loss incurred in 2014 due to portfolio provision releases and reduced levels of defaults in portfolios reflecting a benign UK economy.

Loans and advances grew by £0.4 billion, or 2%, to £20.3 billion. Excluding the transfer of £0.3 billion of Commercial lending back to CPB, lending grew £0.7 billion, or 4%, driven by good growth in both mortgage lending and commercial loans. Customer deposits rose £2.1 billion, or 10%, to £24.1 billion with growth in both transactional accounts and savings accounts.

Central items

	2015 £m	2014 £m
Central items not allocated	(3,271)	(3,780)

Funding and operating costs have been allocated to operating segments based on direct service usage, the requirement for market funding and other appropriate drivers where services span more than one segment.

Residual unallocated items relate to volatile corporate items that do not naturally reside within a segment.

2015 compared with 2014

Central items not allocated represented a charge of £3,271 million compared with a charge of £3,780 million in 2014, representing Treasury and central costs. Other specified items include restructuring costs relating to Williams & Glyn of £630 million, a write-off of intangible assets of £59 million and a loss of £263 million on the repurchase of certain US dollar, Sterling and Euro senior debt securities. Also included are £56 million of income, £109 million of direct operating expenses and £122 million of indirect operating expenses in relation to the international private banking business.

Consolidated balance sheet at 31 December 2015

	2015 £m	2014* £m
Assets		
Cash and balances at central banks	78,999	73,983
Net loans and advances to banks	18,744	23,884
Reverse repurchase agreements and stock borrowing	11,098	20,708
Loans and advances to banks	29,842	44,592
Net loans and advances to customers	306,245	332,951
Reverse repurchase agreements and stock borrowing	28,712	43,987
Loans and advances to customers	334,957	376,938
Debt securities subject to repurchase agreements	20,224	22,923
Other debt securities	59,803	61,351
Debt securities	80,027	84,274
Equity shares	1,069	5,203
Settlement balances	4,108	4,710
Derivatives	263,083	354,582
Intangible assets	6,526	7,765
Property, plant and equipment	4,453	6,123
Deferred tax	2,622	1,881
Prepayments, accrued income and other assets	3,019	4,298
Assets of disposal groups	3,486	81,033
Total assets	812,191	1,045,382
Liabilities		
Bank deposits	31,828	39,066
Repurchase agreements and stock lending	10,266	24,784
Deposits by banks	42,094	63,850
Customer deposits	346,962	357,649
Repurchase agreements and stock lending	27,112	37,350
Customer accounts	374,074	394,999
Debt securities in issue	25,804	41,996
Settlement balances	3,383	4,498
Short positions	20,808	23,028
Derivatives	255,548	350,783
Provisions, accruals and other liabilities	14,070	12,262
Retirement benefit liabilities	3,764	4,289
Deferred tax	729	236
Subordinated liabilities	27,030	30,469
Liabilities of disposal groups	2,980	71,284
Total liabilities	770,284	997,694
Non-controlling interests	54	2,385
Owners' equity	41,853	45,303
Total equity	41,907	47,688
Total liabilities and equity	812,191	1,045,382

*Restated - refer to page 148 for further details

Commentary on consolidated balance sheet

2015 compared with 2014

Total assets of £812.2 billion as at 31 December 2015 were down £233.2 billion, 22%, compared with 31 December 2014. This was driven by the disposal of Citizens, decreases in loans and advances to customers and derivatives assets, reflecting the reshaping of CIB and Capital Resolution run-down.

Loans and advances to banks decreased by £14.8 billion, 33%, to £29.8 billion. Excluding reverse repurchase agreements and stock borrowing ('reverse repos'), down £9.6 billion, 46%, to £11.1 billion, bank placings declined by £5.1 billion, 22%, to £18.7 billion.

Loans and advances to customers declined £42.0 billion, 11%, to £335.0 billion. Within this, reverse repos were down £15.3 billion, 35%, to £28.7 billion. Customer lending decreased by £26.7 billion, 8%, to £306.2 billion, or £37.0 billion to £313.3 billion before impairments. This reflected reductions in CIB together with the run down and disposals in Capital Resolution, partially offset by increases in UK PBB reflecting growth in mortgages and in Commercial Banking which recorded strong new business volumes.

Debt securities were down £4.2 billion, 5%, to £80.0 billion driven mainly by reductions within CIB partially offset by increases in Treasury in the liquidity portfolio.

Equity shares decreased by £4.1 billion, 79%, to £1.1 billion primarily due to the continuing risk reduction and run-down in Capital Resolution.

Movements in the fair value of derivative assets, down £91.5 billion, 26%, to £263.1 billion, and liabilities down, £95.2 billion, 27%, to £255.5 billion, were primarily driven by a reduction in interest rate swap notionals as well as yield curve moves.

Intangible assets decreased by £1.2 billion, 16%, to £6.5 billion mainly due to the write down of £0.5 billion goodwill in Private Banking and the write down of other intangible assets of £0.8 billion, mainly in relation to the reorganisation of CIB.

Property, plant and equipment decreased by £1.7 billion, 27%, to £4.5 billion mainly reflecting disposals and write downs.

The decrease in assets and liabilities of disposal groups down from £81.0 billion to £3.5 billion and £71.3 billion to £3.0 billion respectively, primarily reflects the disposal of Citizens, partially offset by the transfer of the international private banking business to disposal groups.

Deposits by banks decreased by £21.8 billion, 34%, to £42.1 billion, with decreases in repos, down £14.5 billion, 59%, to £10.3 billion and decreases in bank deposits of £7.2 billion, 19%, to £31.8 billion, reflecting the reshaping of CIB and Capital Resolution run-down.

Customer accounts decreased by £20.9 billion, 5%, to £374.1 billion. Within this, repos decreased by £10.2 billion, 27%, to £27.1 billion. Customer deposits were down £10.7 billion, 3%, at £347.0 billion, primarily reflecting the reduction of corporate deposits in CIB and run-down in Capital Resolution offset by growth in UK PBB and in Commercial Banking.

Debt securities in issue decreased by £16.2 billion, 39%, to £25.8 billion, due to a decrease in CIB and in Treasury given the lower funding requirements of a reduced balance sheet.

Subordinated liabilities decreased by £3.4 billion, 11% to £27.0 billion, primarily as a result of the net decrease in dated loan capital with redemptions of £3.6 billion.

Non-controlling interests decreased by £2.3 billion to £54 million, due to the disposal of Citizens.

Owner's equity decreased by £3.5 billion, 8%, to £41.9 billion, primarily driven by the £2.0 billion attributable loss for the year and movements in other reserves.

Cash flow

	2015 £m	2014 £m
Net cash flows from operating activities	1,122	(14,420)
Net cash flows from investing activities	(5,704)	(4,910)
Net cash flows from financing activities	(1,176)	(2,000)
Effects of exchange rate changes on cash and cash equivalents	525	682
Net decrease in cash and cash equivalents	(5,233)	(20,648)

2015

The major factors contributing to the net cash inflow from operating activities of £1,122 million were the increase of £10,787 million in operating assets and liabilities, other provisions charged net of releases of £4,470 million, write down of goodwill and other intangible assets £1,331 million, interest on subordinated liabilities £1,267 million and depreciation and amortisation of £1,173 million. These were partially offset by loans and advances written-off net of recoveries of £8,778 million, other provisions utilised of £2,159 million, elimination of foreign exchange differences of £1,476 million, the operating loss before tax of £1,403 million, profit on sale of subsidiaries and associates of £1,092 million and cash contribution to defined benefit pension schemes of £1,059 million.

Net cash outflows from investing activities of £5,704 million related to the net outflows from purchase of securities of £6,537 million and the purchase of property, plant and equipment of £761 million, offset by inflows of £53 million from disposals primarily Citizens and net cash inflows from the sale of property, plant and equipment of £1,541 million.

Net cash outflows from financing activities of £1,176 million relate primarily to the repayment of subordinated liabilities of £2,279 million and interest paid on subordinated liabilities of £1,313 million partly offset by the proceeds of non-controlling interests issued of £2,491 million.

2014

The major factors contributing to the net cash outflow from operating activities of £14,420 million were the decrease of £11,917 million in operating assets and liabilities, the net loss before tax from continuing and discontinued operations of £855 million, loans and advances written-off net of recoveries of £5,052 million and other provisions utilised of £3,254 million. These were partially offset by the loss on reclassification to disposal groups of £3,994 million and other provisions charged net of releases of £2,478 million.

Net cash outflows from investing activities of £4,910 million related to net investment in business interests and intangible assets of £2,947 million, the net outflows from purchases of securities of £2,314 million, the purchase of property, plant and equipment of £810 million offset by net cash inflows from the sale of property, plant and equipment of £1,161 million.

Net cash outflows from financing activities of £2,000 million relate primarily to the repayment of subordinated liabilities of £4,181 million and interest paid on subordinated liabilities of £1,308 million partly offset by the proceeds of non-controlling interests issued of £2,117 million and the issue of subordinated liabilities of £1,438 million.

Capital and risk management

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Risk overview*

Presentation of information

Except as otherwise indicated by an asterisk (*), information in the Capital and risk management section (pages 28 to 134) is within the scope of the Independent auditor's report. Unless otherwise indicated, disclosures in this section include disposal groups in relevant exposures unless otherwise indicated. Disposal groups in 2015 comprise international private banking business; the first tranche of the sale has been completed and the final tranche is due to complete in the first half of 2016.

2014 disposal groups primarily related to Citizens. Following the deconsolidation of Citizens during 2015, to aid comparison, the 2014 Citizens balances have been presented as a separate line in the disclosures in this section, with the exception of capital management and most liquidity and funding disclosures which remain in line with the relevant regulatory reporting basis. The 2014 comparatives in the Credit risk section exclude Citizens unless otherwise stated.

Capital and risk management are conducted on an overall basis within the RBS Group such that common policies, procedures, frameworks and models apply across the RBS Group. Therefore, for the most part, discussions on these aspects reflect those in the RBS Group as relevant for the business and operations in the Group.

Business model and associated risks

The Group aims to become a bank that its customers and all other stakeholders can trust. It is doing so by focusing on Personal & Business Banking (PBB), Commercial & Private Banking (CPB) and Corporate & Institutional Banking (CIB) customers in its main markets of the UK and the Republic of Ireland. By delivering only services that meet their needs, it aims to achieve an appropriate return. Accordingly, the Group is simplifying its services as well as the processes it uses to deliver them, providing customers with better value services. It aims to become the number one bank in the UK for customer service, trust and advocacy by 2020.

The Group predominantly serves UK and Republic of Ireland customers through retail and commercial banking activities. PBB serves individual and mass affluent customers together with small businesses, providing a variety of traditional retail banking products, including current and savings accounts, residential mortgages and credit cards in the UK through UK PBB and in the Republic of Ireland through Ulster Bank RoI. CPB serves commercial and corporate customers in the UK and Western Europe and high-net-worth individuals, providing loan products and investment services. RBS International serves customers in Jersey, Guernsey, Isle of Man and Gibraltar. CIB serves UK and Western European corporates and global financial institutions through three core business lines: Rates, Currencies and Financing. CIB is moving towards a simpler business model and is re-shaping and downsizing.

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The main sources of earnings are interest income from lending and fee income from transactional and other services. Given increased competition and the low interest rate environment in the UK, the Group's net interest margin has been under pressure. The Group is reducing costs through rationalisation, integration and simplification. A major programme is in train to transform and enhance the ways in which the Group operates.

The Group has made significant progress on the accelerated disposal of selected assets, with the complete divestment of Citizens, the sale of the majority of international private banking businesses, the run-down or sale of RCR assets one year ahead of schedule and a significant proportion of CIB Capital Resolution. Completion of this process will significantly reduce or otherwise improve the profile of credit and market risk faced by the bank. The Group is also committed to full divestment of Williams & Glyn, which provides retail and commercial banking services in the UK, by the end of 2017.

The Group faces regulatory risk and is responding to new and impending regulation. In particular, the Group's business model is adapting to UK Financial Services (Banking Reform) Act requirements that retail banking operations be 'ring fenced' - separated and protected from more volatile undertakings - by 2019.

These divestment, rationalisation and transformation projects expose the Group to a high degree of execution risk over the next few years as it transitions to its target business model. If not effectively managed, this represents a potential management burden and distraction, and associated business upheaval may affect the Group's ability to attract the talent and skills required.

An improved ability to serve customers and other stakeholders through increased focus on key strengths in Western European markets is intended to deliver financial robustness and stronger risk management. However, it does raise geographic and product concentration risks within the Group's target business model. These risks must be managed effectively in increasingly competitive and fast changing target markets, while navigating industry-wide risks such as those related to increasing cyber crime.

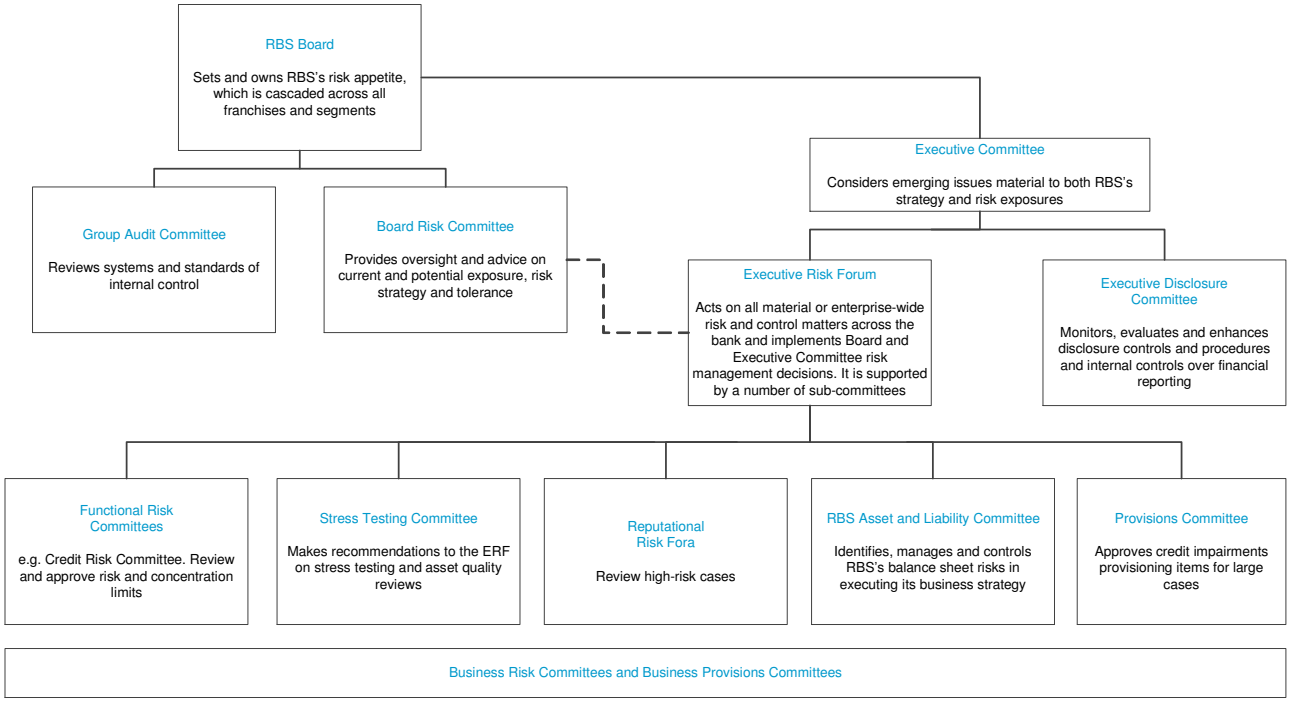
The Group continues to resolve issues related to historical misconduct and unsustainable strategic decision-making. To prevent recurrence of similar issues in the future, the Group aims to underpin its business model with a strong risk culture across its businesses, one that promotes appropriate risk awareness and judgements about risk-taking.

Risk overview* continued

Risk governance

Governance structure

The risk governance structure and the main purposes of each of the committees are set out below:



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Three lines of defence

The three lines of defence model is used industry-wide for the management of risk. It provides a clear set of principles by which to implement a cohesive operating model, one that provides a framework for the articulation of accountabilities and responsibilities for managing risk across the organisation.

First line of defence - Management and supervision

The first line of defence includes customer franchises, Technology and Operations and support functions such as HR, Communications and Financial MI. Responsibilities include:

- Owning, managing and supervising, within a defined risk appetite, the risks which exist in business areas and support functions.
- Ensuring appropriate controls are in place to mitigate risk: balancing control, customer service and competitive advantage.
- Ensuring that the culture of the business supports balanced risk decisions and compliance with policy, laws and regulations.
- Ensuring that the business has effective mechanisms for identifying, reporting and managing risk and controls.

Second line of defence - Oversight and control

The second line of defence includes RBS Group Risk Management and Conduct & Regulatory Affairs (see below for further information), Legal, and the financial control aspects of Finance. Responsibilities include:

- Working with the businesses and functions to develop the risk and control policies, limits and tools for the business to use to discharge its responsibilities.
- Overseeing and challenging the management of risks and controls.
- Leading the articulation, design and development of RBS Group's risk culture and appetite.
- Analysing the aggregate risk profile and ensuring that risks are being managed to the desired level (risk appetite).
- Providing expert advice to the business on risk management.
- Providing senior executives with relevant management information and reports and escalating concerns where appropriate.
- Undertaking risk assurance (see below for more information).

Third line of defence - Internal Audit

Responsibilities include:

- Designing and delivering a risk-based audit plan to provide assurance on material risks and report on whether the RBS Group is managing its material risks effectively.
- Monitoring, evaluating and reporting on the remediation of material risks across the Group.
- Engaging with management and participating in key governance fora to provide perspectives, insights and challenge so as to influence the building of a sustainable bank.
- Advising the Group Audit Committee and executive management with respect to the Group's material risks and their associated controls.
- Reporting any matters which warrant escalation to the RBS Group Board, the Board Risk Committee, Group Audit Committee and the Executive Committee as appropriate.
- Providing independent assurance to the FCA, PRA, CBI and other key jurisdictional regulators on both specific risks and control themes.

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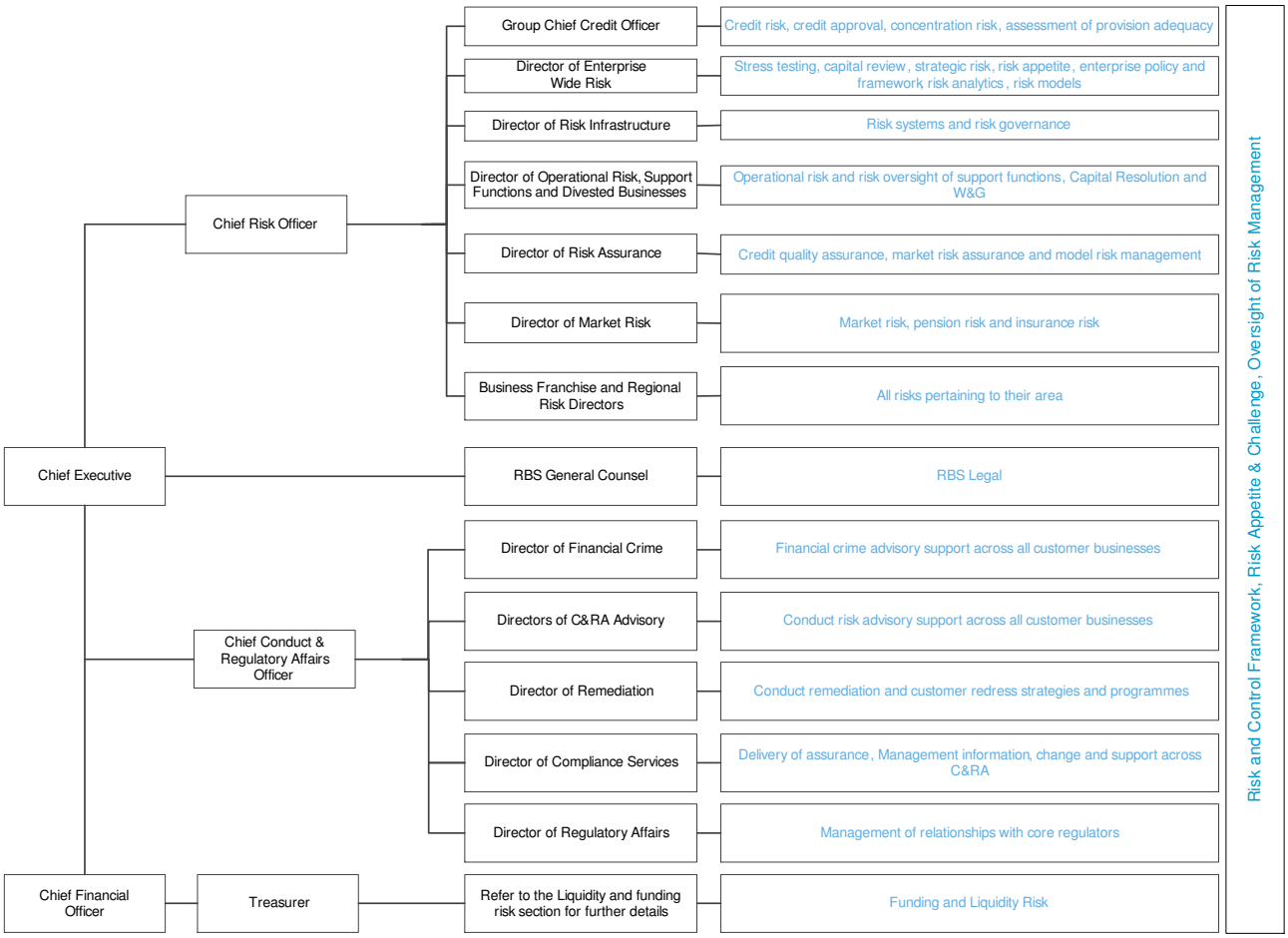
Risk overview* continued

Management structure

RBS Group's management structure and the main elements of each role are illustrated below.



Notes:

(1) RBS Group Risk Management

The RBS Group Chief Risk Officer (CRO) leads RBS Group Risk Management. The CRO reports directly to the RBS Group Chief Executive with an indirect reporting line to the Chairman of the Board Risk Committee and a right of access to the committee's Chairman.

RBS Group Risk Management is a function independent of the franchises, structured by risk discipline to facilitate the effective management of risk.

RBS Group Risk Management is organised into six functional areas: Credit Risk; Enterprise-Wide Risk; Risk Infrastructure; Operational Risk, Support Functions and Divested Businesses; Risk Assurance; and Market Risk. Directors of Risk have been appointed for each of the franchises and for Services. The streamlined structure consolidates risk information, allowing for more efficient decision-making.

The directors of risk functions are responsible for RBS Group-wide risk appetite and standards within their respective disciplines and report to the CRO.

CROs are in place for certain jurisdictions and legal entities to meet local regulatory and governance requirements. They lead the risk management teams locally in support of functional risk heads where teams follow a functional operating model. The key CRO roles report directly to the RBS Group CRO.

Risk committees in the customer businesses and key functional risk committees oversee risk exposures arising from management and business activities and focus on ensuring that they are adequately monitored and controlled.

(2) Conduct & Regulatory Affairs

Conduct & Regulatory Affairs (C&RA) is led by the Chief Conduct & Regulatory Affairs Officer, who reports directly to the Chief Executive and has an indirect reporting line to the Board Risk Committee and a right of access to the committee's chairman. It is responsible for providing oversight of conduct risk and regulatory risk at RBS Group, and does so by setting RBS Group-wide policy and standards, providing advice to each customer business, and ensuring that the mitigating controls are suitable. C&RA also provides leadership of the RBS Group's relationships with its regulators.

The functional heads (the Directors of Financial Crime, Advisory, Remediation, Compliance Services and Regulatory Affairs), report to the Chief Conduct & Regulatory Affairs Officer. Each is responsible, where appropriate, for the RBS Group-wide risk appetite and standards of their respective areas.

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Risk assurance

Risk assurance is a second line of defence function in which most of the RBS Group's risk assurance activities are centralised. These primarily comprise credit risk and market risk quality assurance, controls assurance and Model Risk Management, each of which is described below.

Credit risk and market risk quality assurance: These teams provide assurance to both internal and external stakeholders including the Board, senior management, risk functions, franchises, Internal Audit and the regulators.

Credit risk and market risk quality assurance undertake reviews which assess various aspects of risk as appropriate: including: the quality of risk portfolios; the completeness, suitability, accuracy and timeliness of risk measurements; the quality of risk management practices; policy compliance; and adherence to risk appetite. This includes monitoring the RBS Group's credit portfolios and market risk exposures to assist in early identification of emerging risks, as well as undertaking targeted reviews to examine specific concerns raised either by these teams or by their stakeholders.

The Risk Assurance Committee (RAC) provides governance to ensure a consistent and fair approach to all aspects of the review activities of credit and market risk assurance. Additionally, RAC monitors and validates the ongoing programme of reviews and tracks the remediation of review actions. The credit and market risk assurance teams also attend relevant committees run by the customer franchises and other risk functions to ensure strong communication channels are maintained.

Controls assurance: This team tests the adequacy and effectiveness of key controls relating to credit and market risk, including those within the scope of Section 404 of the US Sarbanes-Oxley Act of 2002. Since the team's creation in late 2014, testing has primarily covered key controls within CIB and CPB.

Model risk management

Model governance

Model governance follows a three lines of defence approach, with model developers having primary accountability and Model Risk Management (MRM) acting in a second-line-of-defence capacity.

MRM is responsible for setting policy, providing governance and insight for all of the RBS Group's statistical, economic, financial or mathematical models and performing independent model validation where necessary. It works with individual businesses to set appropriate model standards, and monitor adherence to these, to ensure that models are developed and implemented appropriately and that their operational environment is fit for purpose.

Going forward, MRM will be responsible for defining and monitoring model risk appetite in conjunction with model developers, monitoring the model risk profile and reporting on the model population and escalating issues to senior management.

The general approach to MRM's independent model validation for risk and pricing models is detailed below. For more specific information relating to market risk models and pricing models, refer to page 129.

Models used within Risk

The Group uses a variety of models as part of its risk management process and activities. Key examples include the use of model outputs to support risk assessments in the credit approval process, ongoing credit risk management, monitoring and reporting, as well as the calculation of risk-weighted assets. Other examples include the use of models to measure market risk exposures and calculate associated capital requirements, as well as for the valuation of positions. The models used for stress testing purposes also play a key role in ensuring the RBS Group holds sufficient capital, even in stressed market scenarios.

For more information on the use of models in the management of particular types of risk, notably credit and market risk, refer to the relevant section.

Independent model validation

MRM performs reviews of relevant risk and pricing models in two instances: (i) for new models or amendments to existing models and (ii) as part of its ongoing programme to assess the performance of these models.

A new model is typically introduced when an existing model is deemed no longer fit for purpose or when exposure to a new product requires a new approach to ensure that risks are appropriately quantified. Amendments are usually made when a weakness is identified during use of a model or following analysis either by the model developers or by MRM.

MRM's independent review comprises some or all of the following steps, as appropriate:

- Testing and challenging the logical and conceptual soundness of the methodology;
- Testing the assumptions underlying the model, where feasible, against actual behaviour. In its validation report, MRM will opine on the reasonableness and stability of the assumptions and specify which assumptions, if any, should be routinely monitored in production;
- Testing whether all key appropriate risks have been sufficiently captured;
- Checking the accuracy of calculations;
- Comparing outputs with results from alternative methods;
- Testing parameter selection and calibration;
- Ensuring model outputs are sufficiently conservative in areas where there is significant model uncertainty;
- Confirming the applicability of tests for accuracy and stability; recalculating and ensuring that results are robust; and
- Ensuring appropriate sensitivity analysis has been performed and documented.

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Risk overview* continued

Based on the review and findings from MRM, the RBS Group's model or risk committees with appropriate delegated authority consider whether a model can be approved for use and whether any conditions need to be imposed, including those relating to the remediation of material issues raised through the review process. Once approved through internal governance, the new or amended model is implemented. Models used for regulatory reporting may additionally require regulatory approval before implementation.

MRM reassesses the appropriateness of approved risk models on a periodic basis according to the approved Periodic Review Policy. Each periodic review begins with an initial assessment. A decision is then made by an internal model governance committee with appropriate delegated authority. Based on the initial assessment, the committee will decide to re-ratify a model based on the initial assessment or to carry out additional work prior to making a decision. In the initial assessment, MRM assesses changes since the last approval along the following dimensions, as appropriate: change in size/composition of the portfolio, market changes, model performance, model changes, status of any outstanding issues, scheduled activities including work carried over from previous reviews.

MRM also monitors the performance of the RBS Group's portfolio of models. By engaging with the business and model users, MRM assesses whether models still capture underlying business rationale appropriately.

Risk culture and appetite

Risk culture

A strong risk culture, as part of a healthy organisational culture, is essential to the realisation of the Group's ambition to build a truly customer-centric bank.

It seeks to create a strong risk culture that becomes part of the way people work and think. Such a culture should be supported by robust practices on risk identification, measurement and management, and on associated controls and governance. Risk competencies, mindsets and behaviours needed to support the RBS Group's risk culture should be embedded across the organisation and made integral to performance reviews.

In 2015, the RBS Group made significant steps in measuring and benchmarking its risk culture across all areas of its activity. This has resulted in agreement on its target risk culture and initiatives needed to achieve it. While changing organisational culture will take time, the RBS Group's risk culture objectives form a key part of individual performance objectives at all levels.

The RBS Group's target risk culture is clearly aligned to its core values of "serving customers", "working together", "doing the right thing" and "thinking long term". They act as a clear starting point for a strong and effective risk culture. Aligned to these values is the Code of Conduct. The Code provides guidance on expected behaviour and sets out the standards of conduct that support the values. It explains the effect of decisions that are taken and describes the principles that must be followed.

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These principles cover conduct-related issues as well as wider business activities. They focus on desired outcomes, with practical guidelines to align the values with commercial strategy and actions. The embedding of these principles facilitates sound decision making and a clear focus on good customer outcomes. They are aligned with the people management and remuneration processes to support a positive and strong risk culture through appropriate incentive structures.

A simple decision-making guide (called the "YES check") has been included in the Code of Conduct. It is a simple, intuitive set of five questions, designed to ensure the values guide day-to-day decisions:

- Does what I am doing keep our customers and RBS safe and secure?
- Would customers and colleagues say I am acting with integrity?
- Am I happy with how this would be perceived on the outside?
- Is what I am doing meeting the standards of conduct required?
- In five years' time would others see this as a good way to work?

Each question is a prompt to think about the situation and the way it fits with the RBS Group's values. The check ensures that employees can think through decisions that do not have a clear answer, guiding the judgements behind their decisions and actions.

If conduct falls short of the Group's required standards, the accountability review process is used to assess how this should be reflected in pay outcomes for those individuals concerned. The Group Performance and Remuneration Committee also consider risk performance and conduct when determining overall bonus pools. The Committee's decisions on pay aim to reinforce the need for good behaviours by all employees.

The RBS Group's policies require that risk behaviour assessment is incorporated into performance assessment and compensation processes for enhanced governance staff.

Risk-based key performance indicators

RBS Group-wide remuneration policy requires remuneration to be aligned with, and to support, effective risk management. The policy ensures that the remuneration arrangements for all employees reflect the principles and standards prescribed by the UK Remuneration Code.

Training

Enabling employees to have the capabilities and confidence to manage risk is core to the RBS Group's learning strategy.

The Group offers a wide range of risk learning across the risk disciplines: Market Risk; Credit Risk; Operational Risk; Enterprise Risk; and Conduct and Regulatory Risk. This training can be mandatory, role specific or for personal development and includes technical and behavioural content.

There is mandatory learning that has to be completed by everyone and is focused on keeping employees, customers and the bank safe. This learning is accessed via the online learning system and is dependent on employee roles and business areas. The system makes it easy for employees to access and complete and allows monitoring at all levels to ensure completion.

Risk appetite

Risk appetite is the way in which the Group expresses the level of risk it is willing to accept in order to achieve its strategic, business and financial objectives.

It is key to ensuring overall safety and soundness and in embedding a strong risk culture throughout the RBS Group.

The Board reviews and approves the risk appetite framework annually, establishing the level and types of risks the RBS Group is able and willing to take in order to meet its:

- Strategic objectives - The strategic plan is built on the core foundations of serving customers well, building a sustainable risk profile and creating long-term value for its shareholders; and
- Wider obligations to stakeholders - If the RBS Group is safe and puts serving customers at the heart of its thinking, it will also perform well for its owners, employees, regulators and communities.

Risk appetite is set for material risks then cascaded and embedded across the RBS Group. It clearly informs, guides and empowers the businesses to execute their strategies within risk appetite.

Strategic risk appetite

The risk appetite framework is designed to ensure the RBS Group remains safe and sound and serves customers and wider stakeholders.

The Board has set out four key strategic risk appetite objectives, aligned with the strategic plan, which provide the boundaries within which the risk appetite for all material risks is set. The strategic risk appetite objectives are:

- Maintain capital adequacy. To ensure there is sufficient capital resources to meet regulatory requirements and to cover the potential for unexpected losses.
- Deliver stable earnings growth. To ensure that strategic growth is based around a longer-term risk-versus reward consideration, the RBS Group sets risk appetite to remain profitable under severe stress.
- Designed to ensure stable and efficient access to funding and liquidity. To ensure that there is sufficient funding to meet its obligations, taking account of the constraint that some forms of funding may not be available when they are most needed.
- Maintain stakeholder confidence. To ensure that the Group is respected, valued and trusted by customers, employees, debt and equity investors, regulators and the wider community to attain its strategic objectives, and establish and maintain an appropriate business culture and operational controls.

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The strategic risk objectives are the bridge between the RBS Group-wide business strategy and the frameworks, limits and tolerances that are used to set risk appetite and manage risk in the business franchises on a day-to-day basis.

Risk appetite measures

Risk appetite starts with the strategic goals set by the RBS Group Board and is then cascaded through key limits and risk tolerances that influence decision-making at all levels.

Risk appetite is set in a manner that:

- Is aligned to business and financial goals. The risk appetite framework ensures that risk is managed in a manner that aligns to and supports the attainment of business and financial objectives.
- Is meaningful to the business. Where possible risk appetite is expressed quantitatively and in a manner that can be cascaded meaningfully and unambiguously to the business. Risk control frameworks and limits set detailed tolerances and limits for managing risk (such as credit risk and market risk) on a day-to-day basis. These limits support, and are required to be consistent with, the strategic risk appetite.
- Considers performance under stress. The establishment and monitoring of risk appetite considers potential risk exposures and vulnerabilities under plausible stress conditions

Effective processes exist for frequent reporting of risks against agreed risk appetite to the Board and senior management.

Risk appetite statements

Risk appetite statements provide clarity on the scale and type of activities permitted, in a manner that is easily communicated.

Risk appetite is set at RBS Group-wide level then cascaded and embedded across all businesses and support functions.

Each franchise, RBS Group-wide material risk owner, function and material legal entity is required to develop, own and manage a risk appetite statement that:

- Evidences alignment with strategic objectives and financial plans.
- Articulates the level of acceptable risk for all risks deemed material.
- Articulates the escalation path to be followed in the instance of a breach in risk appetite.

Risk overview* continued

The communication of risk appetite helps embed appropriate risk-taking in the RBS Group's culture.

Risk control frameworks and limits

Risk control frameworks and their associated limits are an integral part of the risk appetite framework and a key part of embedding risk appetite in day-to-day risk management decisions. The risk control frameworks manage risk by expressing a clear tolerance for material risk types that is aligned to business activities.

The RBS Group Policy Framework directly supports the qualitative aspects of risk appetite, helping to rebuild and maintain stakeholder confidence in the RBS Group's risk control and governance. Its integrated approach is designed to ensure that appropriate controls, aligned to risk appetite, are set for each of the material risks it faces, with an effective assurance process put in place to monitor and report on performance. Risk appetite has its own policy within the RBS Group Policy Framework. This policy sets out clear roles and responsibilities to set, measure, cascade and report performance against risk appetite, and provides assurances that business is being conducted within approved risk limits and tolerances.

*unaudited

Risk coverage

The main risk types faced by the Group are presented below. For further information, refer to pages 40 to 134.

Risk type	How the risk arises	2015 overview (1)
Capital adequacy risk	Capital adequacy risk arises from inefficient management of capital resources.	The PRA monitors capital and leverage on a legal entity basis; the commentary below relates to RBS plc, the most significant legal entity within the Group: • PRA transitional CET1 ratio improved from 13.1% to 16.0% driven by significant RWA reduction, principally in Capital Resolution and fall in CET1 capital reflecting attributable loss of £1.1 billion. The RWA reduction principally reflected strategic balance sheet and risk reduction in CIB and Capital Resolution. • Modelled credit risk RWAs decreased by £24 billion: in corporate exposures (£19 billion) due to CIB portfolio reductions in North American and ongoing GTS exits in Capital Resolution; lower retail exposures (£2 billion) due to risk parameter improvements and disposals of securitisation positions (£2 billion). • Standardised credit risk RWAs including significant investments decreased by £30 billion. This reduction primarily reflected a move from risk-weighting to capital deduction of significant investments in financial institutions, as part of a phased in implementation of end-point CRR. • The de-risking throughout 2015 has allowed the Group to free up capital into the core franchises, helping to align to the strategy of becoming a more focused bank better able to serve our customers in our key markets. • Leverage ratio was 6.9% at 31 December 2015.
Liquidity and funding risk	Liquidity and funding risk arise through the maturity transformation role that the Group performs and arises from day-to-day operations.	• The liquidity position strengthened: the liquidity portfolio of £153 billion at 31 December 2015 covered short-term wholesale funding (STWF) excluding derivative collateral, by more than nine times. STWF including derivative collateral, decreased by £13 billion to £36 billion mainly due to the maturity of term debt issued during the financial crisis. • The liquidity portfolio increased by £4 billion in the year, primarily reflecting the strategic run-down of Capital Resolution loans faster than the associated liabilities and proceeds from the Citizens share sales; this was offset to some extent by UK PBB loan growth. The portfolio includes £61 billion of secondary liquidity consisting of assets eligible for discounting at central banks. The costs associated with maintaining the secondary liquidity portfolio are minimal, being largely administrative and operational costs. • Third party customer loan:deposit ratio reduced to 89% from 95% at the end of 2014. This reflects the strategic run down of Capital Resolution loans and higher retail and commercial deposits, being partly offset by mortgage loan growth in UK PBB.
Business risk	Business risk arises from exposure to, and the ability to assess the impact of, changes in the macro-environment, competition, business operations and technology.	• The Group reduced its business risk profile by implementing its strategic plan to shift the business mix towards the UK and the retail and commercial banking segments, with riskier activities in CIB and Capital Resolution curtailed via disposals and run-down. • The Group continued with its simplification agenda and cost reduction programme.

Note:
(1) Refer to page 294 for abbreviations and acronyms.

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Risk overview* continued

Risk type	How the risk arises	2015 overview
Reputational risk	Reputational risk can arise from the conduct of employees; activities of customers and the countries in which they operate; provision of products and transactions; as well as operations and infrastructure.	• The importance of reputational risk was reinforced with the implementation of a Reputational Risk Policy across business franchises and functions to improve the identification, assessment and management of customers and issues that present a reputational risk. • The most material threats to the Group's reputation continued to originate from historical and more recent conduct issues. As a result, the Group has been the subject of investigations and reviews by a number of its regulators, some of which have resulted in fines and public censure.
Conduct and regulatory risk	Conduct risk arises if customers are not treated in line with their and other stakeholders' expectations. Conduct risk also arises if the Group does not take effective action to prevent fraud, bribery and money laundering. Regulatory risk arises from RBS Group's regulatory, business or operating environments and the Group's response to them.	• Conduct and litigation costs were £3.5 billion in 2015 compared with £2.2 billion in 2014 and included additional provisions of £2.1 billion for historical investment banking activity in the US and £0.6 billion for PPI. The Group continued to remediate historical conduct issues, while also focusing its customer-facing businesses and support functions around the needs of its customers. • A new Conduct Risk Appetite Framework was established. • The Group implemented programmes to prepare for ring-fencing and the UK's new individual accountability regime, as well as other future regulatory requirements; there was significant investment in anti-money laundering controls, governance and training.
Operational risk	Operational risk arises from a failure to manage operations, transactions and assets appropriately. It may arise from human error, an inability to deliver change on time or adequately, or the unavailability of technology services or the loss of customer data. Fraud and theft are sources of operational risk, as is the impact of natural and man-made disasters. It may also arise from a failure to take appropriate measures to protect assets or take account of changes in law.	• The functional operating model for operational risk was embedded, with the aim of ensuring this is managed consistently across RBS Group. This supplemented work by the customer businesses to improve understanding of the operational risk profile and the actions required to mitigate risks outside of appetite. • Following the major IT incident of 2012, there was further significant investment in upgrading the RBS Group's core banking technology infrastructure and in improving a broad range of processes and tools. • The threat to the security of the Group's information from cyber attacks continued to be closely monitored. During 2015, the Group took part in industry-wide cyber attack simulations in order to help test and develop defence planning. Actions taken to mitigate the risk included a large-scale programme to improve user access controls, a reduction in the number of external websites, and enhanced protection against malware. • RBS Group operational risk continued to oversee the execution of major projects, including the transformation plan, the restructuring of CIB and the divestment of Williams & Glyn. This ensured the associated risks were assessed and understood with mitigating activity in place wherever possible.

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Risk type	How the risk arises	2015 overview
Pension risk	The Group is exposed to pension risk through its defined benefit schemes and the variations in their value.	• Following developments in pension accounting and reporting during 2015, the Group revised its policy for determining whether or not it has an unconditional right to a refund of any surpluses in its employee pension funds and also revised prior periods. The incremental impact of this, combined with the one-off accelerated payment made in March 2016, is anticipated to improve the Group's risk profile, capital planning, and resilience through the period to 2019. The accelerated payment is also expected to provide the Main scheme trustee with more flexibility over investment strategy. • Subject to PRA approval, the adverse CET1 capital impact resulting from the accounting policy change and the accelerated payment is expected to be partially offset by a reduction in CET1 capital requirements. Any such core capital offsets are likely to occur at the earliest from 1 January 2017, but they will depend on the PRA's assessment of the Group's CET1 capital position at that time.

Credit risk	Credit risk arises from lending and AFS debt securities. Counterparty credit risk results from derivatives and securities financing transaction activities.	• Overall credit risk exposure decreased in 2015 in line with the Group's strategy to decrease exposure in non-strategic regions. The growth in UK PBB gross mortgage lending reflected our strategy to refocus the business on the UK market, as well as improving economic conditions and increasing house prices in a continuing low interest environment.
		• Risk appetite limits for the sector and product and asset class frameworks were reduced taking account of the revised risk appetite associated with the restructured CIB business.
		• Asset quality improved due to continued focus on reducing risk concentrations and the reduction in exit portfolios driven by the RCR disposal strategy as well as improving economic and market conditions in the UK and Ireland.
		• Deteriorating market conditions in the Oil & Gas and Mining & Metals sectors have led to heightened credit monitoring in these sectors. However, there was no material deterioration in asset quality during 2015 with the majority of the portfolios remaining investment grade.
		• Overall credit metrics strengthened in 2015 principally reflecting Capital Resolution disposals but also the impact of supportive economic conditions:
		  ○ Impairment provisions of £7.1 billion (2014 - £17.9 billion) covered REIL of £12.1 billion (2014 - £28.1 billion) by 59% (2014 - 64%).
		  ○ CRE lending fell to £27.6 billion from £43.3 billion at the end of 2014, of which £3.6 billion (2014 - £13.3 billion) was REIL with provision coverage of 58% (2014 - 68%).

Market risk	The majority of the Group's traded market risk exposure arises in CIB and Capital Resolution through transactions in financial instruments including debt securities, loans, deposits and equities, securities financing and derivatives. The majority of its non-traded market risk exposure arises from retail and commercial banking activities in all franchises from assets and liabilities that are not classified as held for trading.	• RBS plc's average trading internal VaR decreased to £19.0 million (2014 - £26.5 million), and RBSSI's average trading VaR decreased to £1.3 million (2014 - £7.4 million), reflecting strategic exits including from US asset-backed products trading in the first half of 2015. • Non-trading interest rate VaR was significantly lower following the divestment of Citizens. Average interest rate VaR was lower in 2015 as the Group steered its structural interest rate exposure more closely to the neutral duration prescribed by its internal risk management policy. The average VaR was higher than that of RBS Group as some structural interest rate exposures were hedged at a consolidated level.

*unaudited

Capital management*

Definition

Capital management lies at the core of the RBS Group's strength and sustainability goals. The Group defines capital as that part of the liability side of its balance sheet that has the capacity to absorb losses. The construction of capital starts with Common Equity Tier 1 (CET1) and other classes of capital such as Additional Tier 1 (AT1) and Tier 2. The Group will build up sufficient minimum requirements for eligible liabilities (MREL) over the coming years in line with regulatory requirements. Capital management involves the optimisation and efficient use of capital required by businesses, the outcomes of stress testing, the requirements of the market and the regulators and the supply of adequate forms of capital at acceptable prices.

The Prudential Regulatory Authority (PRA) monitors capital and leverage on a legal entity basis. Consequently, quantitative capital, leverage and RWA disclosures for significant legal entities within the Group, primarily RBS plc, NatWest and to a lesser extent Ulster Bank Ireland Limited (UBIL), are included in this section; capital is based on a CRR transitional basis and leverage on CRR Delegated Act including grandfathered Tier 1 instruments.

All the disclosures in this section are unaudited.

Overview and key developments

RBS plc:

- PRA transitional CET1 ratio improved from 13.1% to 16.0% driven by significant RWA reduction, principally in Capital Resolution and fall in CET1 capital reflecting attributable loss of £1.1 billion. The RWA reduction principally reflected strategic balance sheet and risk reduction in CIB and Capital Resolution.
- Modelled credit risk RWAs decreased by £24 billion: in corporate exposures (£19 billion) due to CIB portfolio reductions in North American and ongoing GTS exits in Capital Resolution; lower retail exposures (£2 billion) due to risk parameter improvements and disposals of securitisation positions (£2 billion).
- Standardised credit risk RWAs including significant investments decreased by £30 billion. This reduction primarily reflected a move from risk-weighting to capital deduction of significant investments in financial institutions, as part of a phased in implementation of end-point CRR.
- The de-risking throughout 2015 has allowed the Group to free up capital into the core franchises, helping to align to the strategy of becoming a more focused bank better able to serve our customers in our key markets.
- Leverage ratio was 6.9% at 31 December 2015.

NatWest Plc:

- CET1 ratio decreased from 13.9% to 11.6%, reflecting the current year loss of £1.4 billion, consisting of PPI provisions of £0.4 billion and the impairment of investments in US related subsidiaries, of £1.6 billion following additional provisions relating to US RMBS litigation. The loss on remeasurement of the retirement benefit schemes resulted in a CET1 capital reduction of £1.4 billion, which was partially offset by a capital injection of £800 million from RBS plc.
- Modelled credit risk RWAs decreased by £1.5 billion, primarily Retail as a result of risk parameter improvements in PBB.
- Standardised RWAs decreased by £6 billion primarily reflecting a move from risk weighting to capital deduction of significant investments in financial institutions, as part of phased in implementation of end-point CRR.
- Leverage ratio was 4.7% at 31 December 2015.

UBIL:

- CET1 ratio improved from 17.3% to 29.6%. 2015 CET1 ratio benefited from the inclusion of £0.9 billion of 2014 profit.
- RWAs were £5.0 billion lower with the contributors being the reduction in the tracker mortgage portfolio, lower Central Bank of Ireland add-on for corporate exposures and exchange rate measurements.
- Leverage ratio was 24.0 % at 31 December 2015 reflecting the strong capital position.

Risk appetite and strategy

Risk appetite

The RBS Group's risk appetite framework establishes appetite targets on quantitative and qualitative measures which are set by the Board, aligned with its key strategic risk objectives. Capital risk appetite is set at the holding company level and cascaded to material subsidiaries to help inform capital targets alongside other quantitative measures such as Individual Capital Guidance set annually by the PRA.

The Group has a capital management framework including policies and procedures that are designed to measure actual and projected capital performance against risk appetite, ensures that it continues to comply with regulatory requirements and is positioned to meet anticipated future changes to its capital requirements. The RBS Group's capital risk appetite at the holding company level, which informs its capital targets at subsidiary levels, is reviewed and set annually by the Board. Capital risk appetite sets target ratios for CET1 and leverage under stress scenarios and reverse stress tests. These then inform capital targets.

The RBS Group also looks at other factors that may impact capital targets such as double leverage, distributable reserves, capital headroom to Maximum Distributable Amount (MDA) and intra group limits and exposures. Risk appetites are also set at legal entity level and may encompass additional specific risk measures such as intra group exposures and limits and double leverage.

*unaudited

Strategy

The Group maintains a sufficient level of capital that allows it to operate over its strategic horizon with an agreed risk appetite in pursuit of its business strategy, taking into account regulatory requirements, support for customers and to provide confidence to stakeholders.

The RBS Group is able to accumulate additional capital through the reduction in RWAs (either through disposals or natural attrition) accumulation of profits over time, by raising new equity via, for example, a rights issue or debt exchange and by raising AT1 and Tier 2 capital by issuing subordinated liabilities at the holding company level and downstreaming to subsidiaries such as RBS plc. The cost and availability of additional capital is dependent upon market conditions and perceptions at the time. The RBS Group is also able to manage the demand for capital through management actions including adjusting its lending strategy, risk hedging strategies and through business disposals.

The level of CET1 at the consolidated level and within specific legal entities is the cornerstone of capital strategy. Complementing CET1, the RBS Group issues externally and will allocate internally AT1 capital, Tier 2 capital and looking forward, MREL instruments in accordance with internal needs, regulatory requirements and strategic plans. The amount of additional capital is determined as part of the annual budgeting cycle, by market conditions and through ongoing dialogue with regulators. It is under constant review and evaluation to ensure that it provides efficient and optimally valued benefits at all times.

The capital raising strategy is driven by two factors: the optimal blend to satisfy regulatory requirements, and the most cost effective means of financing. The RBS Group has a range of instruments available to it both internally and externally. It also has legacy capital instruments that may still have some transitional benefits under the changing regulatory framework. The RBS Group constantly looks at the value and efficiency provided by those instruments and will take such market related actions to the extent that circumstances and conditions merit such action. The RBS Group's policy is to manage its externally issued portfolio of debt securities for value.

*unaudited

Capital management* continued

Framework and governance

The framework for capital management within the RBS Group first looks at the sources and drivers of risk based capital requirements. Through the internal budget and planning cycle, and increasingly through stress testing, each franchise balances the blend of products that is offered to customers, having regard to the impact of each on capital and leverage against the backdrop of the overall business strategy. Capital and risk management, including capital planning (refer to page 43), stress testing and ICAAP are conducted on an overall basis within the RBS Group such that common frameworks and models apply across the RBS Group. Therefore, for the most part, discussions on these aspects reflect those in the RBS Group as relevant for the businesses and operations in the Group.

A number of tools and processes taken together contribute to an integrated view of capital management. The diagram below is used to present this view:

Governance

The RBS Group Board sets the strategic direction and ensures that the RBS Group manages risk effectively by approving and monitoring its strategic risk appetite, considering RBS Group-wide stress scenarios and agreed mitigants, as well as identifying longer-term strategic threats to the business operations. The Board also approves the ICAAP.

Capital planning

The RBS Group uses the budgeting cycle to forecast future capital requirements at CET1, Tier 1, Tier 2 and total capital levels including MREL at both holding company level and major operating entity level. Forecasts are measured against minimum regulatory requirements and specific regulatory guidance such as the Individual Capital Guidance.

Strategic considerations in the medium-term capital plan will be driven by key impacts such as a more restrictive approach to the capital base, higher capital ratio targets and enhanced risk coverage.

Stress Testing (and use of)

This is an integral part of capital planning. Stress testing results are produced through the same capital planning and stress testing models used for the budgeting and monthly review.

In addition to informing the ICAAP, stress testing in the RBS Group is a key risk management tool used to support strategic financial planning, risk appetite, risk identification and risk mitigation.

Stress testing results are presented to senior management (and BRC/Board) periodically, and used to assess capital impacts of business decisions

Recovery and resolution planning

The RBS Group prepares an annual recovery plan, which include a framework of indicators identifying the points at which appropriate actions may be taken in the event of unexpected weaknesses in its capital or liquidity resulting from either idiosyncratic or systemic stress, as well as a menu of options for addressing such weaknesses. The RBS Group's 2015 Recovery Plan was prepared in line with the PRA's requirement that banks prepare, maintain and review recovery plans.

Internal Capital Adequacy Assessment Process (ICAAP)

The ICAAP assesses the RBS Group's material risks determining how much capital is required to cover these risks. The ICAAP consists of two types of internal capital assessment:

- a Point-in-time capital assessment as at the financial year end; and
- a Forward-looking stress capital assessment.

The final ICAAP is approved by the RBS Group Board prior to submission to the PRA.

Assessing, monitoring and maintaining adequate capital. It is the RBS Group's policy to build and sustain a strong capital base and to use it efficiently throughout its activities to support strategic objectives and optimise shareholder returns while maintaining a prudent relationship between its capital base and the underlying risks of the business, including the risk of excessive leverage.

Board Risk Committee (BRC)

With sight of various risk types the RBS Group Board Risk Committee (BRC) is responsible for providing oversight and advice to the Board in relation to current and potential future risk exposures of the RBS Group and future risk strategy, including determination of risk appetite and tolerance.

Capital Risk Assessment (CRA)

CRAs are annual 'top down' processes to help identify, understand and assess material risks. Consideration is given to whether and how much capital should be set aside against each risk type forming a key input to the ICAAP. For effective risk management CRAs are marked against financial or non-financial thresholds.

*unaudited

Capital planning

Capital and leverage is actively managed and regulatory ratios are a key factor in the RBS Group's planning processes and stress analyses. Capital planning is an activity undertaken within Treasury to determine the appropriate amount of capital needed over the budget horizon under both base and stress projections using both risk and leverage based assessment tools and given a specific risk appetite.

Capital plans are derived for the RBS Group overall and its major operating and regulated entities. Capital plans are prepared in compliance with specific regulatory rules (for example CRD IV) and in accordance with system wide and local, specific regulatory guidance. Capital plans for UK regulated entities are drawn up centrally whereas capital plans for non-UK regulated entities are drawn up locally and subject to central review and challenge to ensure consistency of approach and adherence to capital management policies. Capital plans take into account any funding arrangements between the holding company entity and operating entities. The RBS Group is transitioning to a single point of entry (SPE) structure under the Independent Commission on Banking's (ICB's) ring fencing requirements. This creates a need to actively manage any legacy securities issued externally by the operating entities and any internal funding arrangements between entities, particularly the holding company.

The starting point for any capital plan will be with the annual budget cycle which forecasts the Group's balance sheet trajectory over a 5 year forward looking horizon. The budget cycle will incorporate assumptions about the future shape and direction of the balance sheet of the RBS Group and its operating entities. It will include assumptions around the future path of RWAs, profitability and tax. Idiosyncratic factors such as conduct and litigation costs and disposals are also considered. Finally known or expected system or firm specific regulatory guidance (for example phasing in of CRD IV assumptions or leverage requirements) are also considered.

The capital plans are tested for capital adequacy and measured against the RBS Group's risk appetite framework using a range of stress scenarios covering adverse economic conditions as well as other adverse factors that could impact the bank. In addition the RBS Group maintains a recovery plan which sets out a range of potential mitigating actions that could be taken in response to an extreme stress. Known and expected assumptions around the future direction of regulation is also taken into account. Furthermore specific idiosyncratic risks such as conduct risk are factored into capital plans.

From these inputs a forecast will be derived on how much capital is required to support these assumptions using both risk and leverage based approaches. This will estimate the required amount of CET1 through to non-capital minimum requirement eligible liabilities (MREL) in each period over the forecast.

Capital policies and procedures are subject to independent oversight. Regular reporting of actual and projected capital and leverage ratios, including those in stressed scenarios, is undertaken, including submissions to the RBS Group's ALCo, ERF, EXCo, Board Risk Committee and the Board.

Once the capital plan is approved it is then subject to ongoing review and assessment to reflect changes to the underlying components such as forecasts or new regulatory guidance or assumptions. Shorter term forecasts are more frequently undertaken to understand and respond to variations of actual performance against the plan.

The regulatory framework within which the RBS Group operates continues to be developed at a global level through the FSB and Basel Committee, at a European level mainly through the issuance of CRD IV technical standards and guidelines and within the UK by the PRA and through directions from the FPC. The RBS Group continues to monitor regulatory developments very closely, analysing the potential capital impacts to ensure it continues to maintain a strong capital position that exceeds the minimum regulatory requirements and risk appetite and is consistent with market expectations.

Capital requirements: Pillar 1 and 2

Capital demand is normally the aggregation of Pillar 1, Pillar 2A, the greater of the CRD IV or Pillar 2B buffers, and any management buffer (for example over and above MDA). Pillar 2 is becoming an increasingly important component of our capital requirements.

Pillar 2A is determined through the ICAAP process mentioned herein and reflects RBS Group specific risks. Factors driving Pillar 2 requirements include operational risk, interest rate risk in the banking book, credit concentration risk and pension risk amongst others.

The Pillar 2B requirement and recently introduced PRA buffer reflects the impact of stress through the analysis undertaken in annual ICAAP. The amount of stress capital may well also be informed by performance under the new regulatory stress testing process. The amount of stress based capital requirement is the higher of Pillar 2B or the CRD IV risk buffers plus any management buffer.

A management buffer may be overlaid on top of that to reflect additional risks that the RBS Group Board believe are prudent to cover (such as headroom over and above any MDA threshold).

Capital supply

Capital supply consists of the amount of CET1, AT1, Tier 2 and, going forward, non-capital MREL securities in existence at any one time. The capital planning process determines the most efficient mix between these different types of security in keeping with the RBS Group's strategic plans and risk appetite. Considerations include:

- Internal risk appetite (including stress testing);
- Regulatory policies and guidance; and
- Market conditions and expectations.

*unaudited

Capital management* continued

The RBS Group will issue capital securities from time to time and may engage in selective buy backs, liability management exercises and other market actions in line with its stated risk appetite and other metrics. The RBS Group's policy is to manage its externally issued portfolio of debt securities for value.

Regulatory developments and the RBS Group's current and future capital position

Regulatory proposals and rules issued or set by the following regulators are the most relevant for the RBS Group:

- Basel - recommendations for all major international institutions - usually through Basel Committee of Banking Supervision (BCBS);
- EU - issue consistent rules for all EU banks and investment firms, commonly through the European Banking Authority (EBA); and
- PRA - additional local rules for UK banks and investment firms.

Capital

Following the implementation of the Basel III proposals through the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD), collectively known as CRR/CRD IV, which came into effect on 1 January 2014, the regulatory drive towards improved capital standards for banks continues and is centred on three broad themes:

- Robust definitions of capital for CET1 and leverage purposes that are not dependent on one or more economic cycles;
- Improved strength of banks, with strategic plans and business models capable of undergoing one or more significant stress events; and
- Valid and viable recovery plans in place for banks to return to normality after a period of stress or, easy application of the resolution frameworks.

Many of these aspects still require analysis and debate and therefore any implementation is likely to take many years. CRR/CRD IV introduced the following minimum requirements to be met by 2019:

- Pillar 1 requirement of: CET1 of 4.5% of RWAs; Tier 1 of 6%; and total capital of 8%;
- CRD IV Combined buffers: capital conservation buffer of 2.5% of RWAs; countercyclical capital buffer of up to 2.5%; GSIB surcharge of 1.0% for the RBS Group based on the most recent determination from the FSB; and

The PRA policy statement PS7/13 outlined changes to the minimum level of CET1 capital for large UK banks as follows:

- The PRA required UK banks to meet the CRD IV end point Pillar 1 requirement from 1 January 2015;
- All Pillar 2A risks must be met with at least 56% CET1 capital. This matches the proportion of CET1 capital required for Pillar 1. The remaining (44%) allocation of Pillar 2A is restricted to 19% Tier 1 and 25% Tier 2; and
- All regulatory deductions from capital align CET1 with the end-point CRR definition, effectively making fully loaded Basel III the regulatory definition.

*unaudited

The PRA issued Policy Statement 17/15 in July 2015 setting out the Pillar 2 capital requirements for UK banks. The changes are intended to support a more risk sensitive and consistent approach to setting Pillar 2A (P2A) capital and to provide greater transparency of the PRA capital setting process by allowing firms to manage present and future regulatory capital demands. Implementation is from 1 January 2016 in line with the CRD IV capital conservation and systemic buffers and the European Banking Authority's Supervisory Review and Evaluation Process guidelines. The changes are as follows:

- The variable element of P2A is now expressed as a percentage of RWAs plus fixed add-ons instead of the current method where P2A is a formula comprising both a variable and a fixed element;
- The PRA buffer, presently applicable only for the RBS Group replaces the current Capital Planning Buffer (CPB). Use of the buffer will not be a breach in capital requirements and will not result in capital distribution restrictions however, failure to meet Pillar 2B (P2B) buffer may result in enhanced supervisory action;
- The P2B buffer, presently applicable only for RBS Group, is now calculated as a percentage of RWAs rather than absolute terms and is to be met with CET1;
- Firms already subject to a CPB are required to meet P2B with CET1 in full immediately;
- Where the PRA considers that firms have weak risk management or governance, PRA may require firms to hold additional PRA buffer on a scalar ranging from 10-40% of a firm's CET1 Pillar 1 plus P2A capital requirements; and
- Firms have the discretion to publicly disclose their aggregate P2A charge from 1 January 2016. Component parts of P2A and the PRA buffer remain confidential.

Leverage

The RBS Group's Leverage ratio requirements are also subject to the following key aspects (consistent with proposals outlined in PS27/15 - 'Implementing a UK leverage ratio framework'):

- Minimum Tier 1 leverage ratio of 3%. To be met 75% by CET1 and a maximum 25% fully CRDIV compliant AT1;
- A supplementary leverage buffer applying to GSIBs equal to 35% of the corresponding risk-weighted systemic risk buffer rates to be met with CET1; and
- A countercyclical leverage ratio buffer equal to 35% of the risk-weighted countercyclical capital buffer rate to be met from CET1. The countercyclical buffer is currently set at 0%.

Stress testing

In October 2015, the BoE published its approach to stress testing of the UK banking system out to 2018. The publication outlines the following key features of the BoE approach:

- A cyclical scenario to assess the risks to the banking system based on the financial cycle.
- The severity of the scenario to be counter-cyclical in nature.
- Every second year, the BoE will complement the annual testing with an additional exploratory scenario to probe the resilience of the system to risks not easily linked to the financial cycle.

- The BoE intends to include an integrated framework for decision-making around the setting of capital buffers, as well as a clear and transparent process for determining whether banks need to strengthen their capital positions.
- A hurdle rate framework is to be enhanced, and will align to the overall capital framework. Within the hurdle rate, a bank will be expected to meet all of its minimum risk-based CET1 capital requirements (Pillar 1) in the scenario, as well as Pillar 2A CET1 requirements. Additionally, GSIB buffers will be included in the hurdle rate.

As a major UK bank, the RBS Group will be included in the annual cyclical scenarios and may also be required to participate in the biennial exploratory scenario stress tests to the extent that the risks being probed are relevant to it.

MREL and TLAC

The banking resolution and recovery directive introduces requirements for banks to maintain at all times a sufficient aggregate amount of own funds and eligible liabilities (that may be bailed in using the bail-in tool), known as the minimum requirements for eligible liabilities (MREL). The aim is that the minimum amount should be proportionate and adapted for each category of bank on the basis of their risk or the composition of their sources of funding.

The EBA noted that the technical standards would be compatible with the proposed term sheet published by the FSB on TLAC requirements for GSIBs, but there remains a degree of uncertainty as to the extent to which MREL and TLAC requirements may differ.

Following the FSB finalising its TLAC proposals in November 2015, the PRA published its proposed requirements for MREL which will be the way in which the UK implements the TLAC standard. MREL will apply to GSIBs from 2019 and to other relevant UK firms from 2020. The purpose of MREL is to ensure that, in the event of failure, a bank has sufficient loss-absorbing and recapitalisation capacity to allow for an orderly resolution that minimises any adverse impact on financial stability whilst preventing public funds being exposed to loss. The requirements will be firm-specific but the PRA's consultation paper proposes that MREL will be required:

- At a consolidated and individual bank level, including for the holding entity of a banking group.
- At an amount at least equal to two times the current minimum Pillar 1 and Pillar 2A capital requirements, or, if higher, any applicable leverage ratio requirement, or the minimum capital requirements under Basel plus any applicable CRD IV capital buffers: once for loss absorbency, once for recapitalisation.

The US Federal Reserve has proposed rules which will require US bank holding companies and intermediate holding companies of foreign banks to hold specified amounts of both long term debt and TLAC from January 2019. The RBS Group is considering the impact of these rules.

*unaudited

Systemically Important Banks

In November 2015, the RBS Group was moved down to the lowest bucket for required loss absorbency in the FSB's updated list of GSIBs. Regulatory proposals relating to Domestically Systemically Important Banks (DSIBs) and Other Systemically Important Institutions (OSII) continue to progress and could impact the level of CET1 required to be held by the RBS Group and specific legal entities including NatWest and the Royal Bank.

Regulatory proposals relating to Domestically Systemically Important Banks (DSIBs) and Other Systemically Important Institutions (OSII) continue to be progressed and could impact the level of CET1 that is required to be held by the RBS Group and specific legal entities including NatWest and the Royal Bank. The EBA published in December 2014 a quantitative methodology as to how European regulators could quantify which firms would qualify as DSIBs. The PRA published CP39/15 on this in October 2015, and published its list of the sixteen firms designated as OSII; the RBS Group is included within this list.

Systemic risk buffer (SRB)

In January 2015, HM Treasury issued an explanatory memorandum on the SRB for banks, building societies and investment firms. The regulation implements Articles 133 and 134 of Directive 2013/36/EU and addresses the outstanding capital buffer element of the ring-fencing policy recommended by the ICB and agreed by the UK Government.

The purpose of the SRB is to prevent and mitigate long term non-cyclical systemic or macro prudential risks not covered by existing regulation where there is potential for serious negative consequences for the financial system and real economy

The SRB will apply to large banks with core (ring fenced entity) deposits of more than £25 billion and large building societies with deposits of more than £25 billion. Implementation will occur from 1 January 2019 and capital buffers will range from 0-3% of a firm's RWAs.

Capital management* continued

On 29 January 2016, the FPC proposed that those banks and building societies with total assets above £175 billion will be set progressively higher SRB rates as total assets increase through defined buckets. HM Government required the FPC to produce a framework for the SRB at rates between 0% and 3% of RWAs. Under the FPC's proposals, ring-fenced bank sub-groups and large building societies in scope with total assets below £175 billion will be subject to a 0% SRB. Based on current information, under these proposals the FPC expects the largest ring-fenced bank in 2019 to have a 2.5% SRB. In line with the FPC's previous announcement on the leverage ratio framework, those institutions subject to the SRB will also be set a 3% minimum leverage ratio requirement, together with an additional leverage ratio buffer calculated at 35% of the applicable SRB rate. For example, an institution with an SRB rate of 1% would have an additional leverage ratio buffer of 0.35%. The proposed calibration is expected to add around an aggregate 0.5 percentage points of risk-weighted assets to equity requirements of the system in aggregate. The PRA will be responsible for applying the framework and will have ultimate discretion over which firms must hold the buffer and its specific size.

Ring-fencing

- The UK Financial Services (Banking Reform) Act passed into UK law in December 2013 implementing recommendations of the ICB. The PRA is in the process of finalising its rules with respect to ring-fencing.
- The PRA is consulting on the need for firms to hold capital resources equivalent to at least 25% of annual fixed overheads in respect of critical services to facilitate operational continuity in resolution.

*unaudited

Measurement

Capital, RWAs and leverage

Under Capital Requirements Regulation (CRR), regulators within the European Union monitor capital and leverage on a legal entity basis, with local transitional arrangements on the phasing in of end-point CRR. The capital resources, leverage and RWAs based on the relevant transitional basis for the significant legal entities within the Group are set out below.

	2015			2014 (1)		
Capital (2)	RBS plc £bn	NatWest Plc £bn	UBIL £bn	RBS plc £bn	NatWest Plc £bn	UBIL £bn
CET1	32.4	7.2	5.7	34.5	9.5	4.2
Tier 1	34.7	7.2	5.7	36.7	9.6	4.2
Total	51.3	12.1	6.2	55.3	14.8	4.7
RWAs						
Credit risk						
- non-counterparty	146.4	54.4	17.8	200.1	61.7	22.5
- counterparty	21.8	0.4	0.3	27.7	0.6	0.4
Market risk	19.1	0.6	—	19.0	0.5	—
Operational risk	15.6	6.4	1.1	17.1	5.5	1.3
	202.9	61.8	19.2	263.9	68.3	24.2
Risk asset ratios	%	%	%	%	%	%
CET1	16.0	11.6	29.6	13.1	13.9	17.3
Tier 1	17.1	11.6	29.6	13.9	14.0	17.3
Total	25.3	19.6	32.1	20.9	21.7	19.5

Leverage	2015		
Tier 1 capital (£bn)	34.7	7.2	5.7
Leverage (£bn)	502.6	153.1	23.7
Leverage ratio (%)	6.9	4.7	24.0

Notes:
(1) Capital and leverage ratios have not been impacted by the pension accounting policy change.
(2) Capital Requirements Regulation (CRR) as implemented by the Prudential Regulation Authority in the UK, with effect from 1 January 2014. All regulatory adjustments and deductions to CET1 have been applied in full for with the exception of unrealised gains on available-for-sale (AFS) securities which has been included from 2015 under the PRA transitional basis.
(3) UBIL 2014 profit (unverified for regulatory reporting purposes in 2014) is excluded from 2014 but included in 2015.

General:
In accordance with the PRA's Policy Statement PS7/2013 issued in December 2013 on the implementation of CRD IV, all regulatory adjustments and deduction to CET1 have been applied in full (end-point CRR) with the exception of unrealised gains on AFS securities which will be included from 2015 (PRA transitional basis).

From 1 January 2015, RBS must meet at least 56% of its Pillar 2A capital requirement with CET1 capital and the balance with Additional Tier 1 and/or Tier 2 capital. The Pillar 2A capital requirement is the additional capital that RBS must hold, in addition to meeting its Pillar 1 requirements in order to comply with the PRA's overall financial adequacy rule.

Measures in relation to end-point CRR basis, including RWAs, are based on the current interpretation, expectations, and understanding, of the CRR requirements, as well as further regulatory clarity and implementation guidance from the UK and EU authorities (end-point CRR basis). The actual end-point CRR impact may differ when the final technical standards are interpreted and adopted.

Capital base:
(1) Own funds are based on shareholders' equity.
(2) The adjustment arising from the application of the prudent valuation requirements to all assets measured at fair value, has been included in full. The prudential valuation adjustment relating to assets under advanced internal ratings approach has been included in impairment provisions in the determination of the deduction from expected losses.
(3) Where the deductions from AT1 capital exceed AT1 capital, the excess is deducted from CET1 capital. The excess of AT1 deductions over AT1 capital in year one of transition is due to the application of the current rules to the transitional amounts.
(4) Insignificant investments in equities of other financial entities (net): long cash equity positions are considered to have matched maturity with synthetic short positions if the long position is held for hedging purposes and sufficient liquidity exists in the relevant market. All the trades are managed and monitored together within the equities business.
(5) Based on our current interpretations of the Commission Delegated Regulation issued in December 2013 on credit risk adjustments, standardised latent provision has been reclassified to specific provision and is not included in Tier 2 capital.

Risk-weighted assets (RWAs):
(1) Current securitisation positions are shown as risk-weighted at 1,250%.
(2) RWA uplifts include the impact of credit valuation adjustments and asset valuation correlation on banks and central counterparties.
(3) RWAs reflect implementation of the full internal model method suite, and include methodology changes that took effect immediately on CRR implementation.
(4) Non-financial counterparties and sovereigns that meet the eligibility criteria under CRR are exempt from the credit valuation adjustments volatility charges.
(5) The CRR final text includes a reduction in the risk-weight relating to small and medium-sized enterprises.

*unaudited

Capital management* continued

Capital resources

	2015			2014		
	RBS plc £m	NatWest Plc £m	UBIL £m	RBS plc £m	NatWest Plc £m	UBIL £m
Shareholders' equity						
Shareholders' equity	51,177	11,282	5,753	52,553	13,312	5,081
Preference shares - equity	(1,421)	—	—	(1,421)	—	—
	49,756	11,282	5,753	51,132	13,312	5,081
Regulatory adjustments and deductions						
Own credit	17	—	—	659	—	—
Defined benefit pension fund adjustment	(138)	—	142	(127)	—	320
Cash flow hedging reserve	(286)	1	—	(755)	3	—
Deferred tax assets	(252)	(622)	(210)	(258)	(742)	—
Prudential valuation adjustments	(349)	(1)	—	(324)	(1)	—
Goodwill and other intangible assets	(544)	(498)	—	(917)	(530)	—
Expected losses less impairments	(395)	(703)	(22)	(805)	(785)	(3)
Instruments of financial sector entities where the institution has a significant investment	(15,680)	(2,413)	—	(14,809)	(2,318)	—
Significant investments in excess of secondary capital	—	(424)	—	—	—	—
Other regulatory adjustments	287	532	27	703	529	(1,217)
	(17,340)	(4,128)	(63)	(16,633)	(3,844)	(900)
CET1 capital	32,416	7,154	5,690	34,499	9,468	4,181
Additional Tier 1 (AT1) capital						
Qualifying instruments and related share premium subject to phase out	3,493	204	—	3,503	234	—
Tier 1 deductions						
Instruments of financial sector entities where the institution has a significant investment	(1,175)	(187)	—	(1,291)	(140)	—
Tier 1 capital	34,734	7,171	5,690	36,711	9,562	4,181
Qualifying Tier 2 capital						
Qualifying instruments and related share premium	19,039	5,058	492	20,427	5,380	528
Tier 2 deductions						
Instruments of financial sector entities where the institution has a significant investment	(2,432)	(92)	—	(1,836)	(102)	—
Other regulatory adjustments	—	—	(7)	(41)	(8)	(5)
	(2,432)	(92)	(7)	(1,877)	(110)	(5)
Tier 2 capital	16,607	4,966	485	18,550	5,270	523
Total regulatory capital	51,341	12,137	6,175	55,261	14,832	4,704

Note:
(1) Regulatory capital for 2014 has not been impacted by the change in accounting policy for pensions.

*unaudited

Leverage exposure

The leverage exposure is based on the CRR Delegated Act.

	2015		
Leverage	RBS plc £bn	NatWest Plc £bn	UBIL £bn
Derivatives	265.6	2.1	0.7
Loans and advances	175.9	207.6	19.9
Reverse repos	31.1	—	—
Other assets	196.6	10.7	2.2
Total assets	669.2	220.4	22.8
Derivatives			
- netting	(260.1)	(1.4)	(0.1)
- potential future exposures	76.8	0.2	0.2
Securities financing transactions gross up	5.2	—	—
Undrawn commitments	46.3	9.9	1.0
Regulatory deductions and other adjustments	(15.9)	(5.2)	(0.2)
Exclusion of core UK-group exposures	(18.9)	(70.8)	—
Leverage exposure	502.6	153.1	23.7

*unaudited

Liquidity and funding risk

Definition

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

All the quantitative disclosures in this section are audited. Certain disclosures exclude Citizens for 2014 to allow like-for-like comparison with 2015.

Sources of funding and liquidity

The risk arises through the maturity transformation role that banks perform. It is dependent on Group specific factors such as maturity profile, composition of sources and uses of funding, the quality and size of the liquidity portfolio as well as broader market factors, such as wholesale market conditions alongside depositor and investor behaviour.

The Group's primary funding source is its customer deposit base, primarily built through its retail and commercial franchises in the UK and Ireland. These deposits form a stable base which fully funds the Group's customer lending activities.

Complementary to its deposit funding, the Group maintains access to various wholesale markets for funding, on both a public and private basis, across a range of currencies, geographies and maturities. These include long-term secured and unsecured debt, short-term money markets and repurchase agreements. The RBS Group has set policies for the prudent use of wholesale funding, as part of its wider liquidity policies.

The Group accesses the wholesale funding markets directly or through its main operating subsidiaries via established funding programmes. The use of different entities to access the market from time to time allows the Group to further diversify its funding mix and in certain limited circumstances demonstrate to regulators that specific operating subsidiaries enjoy market access in their own right.

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

Overview and key developments

- The liquidity position strengthened with the liquidity portfolio of £153 billion at 31 December 2015 covering short-term wholesale funding (STWF) excluding derivative collateral, by more than nine times. STWF including derivative collateral, decreased by £13 billion to £36 billion mainly due to the maturity of term debt issued during the financial crisis.
- The liquidity portfolio increased by £4 billion in the year, primarily reflecting the strategic run-down of Capital Resolution loans faster than the associated liabilities and proceeds from the Citizens share sales; this was offset to some extent by UK PBB mortgage loan growth. The portfolio includes £61 billion of secondary liquidity consisting of assets eligible for discounting at central banks. The costs associated with maintaining the secondary liquidity portfolio are minimal being largely administrative and operational costs.
- The customer loan:deposit ratio reduced to 89% compared with 95% at the end of 2014. This reflects the strategic run down of Capital Resolution loans and higher retail and commercial deposits, partly offset by loan growth within UK PBB.

Policy, framework and governance

Internal liquidity policies are designed to ensure that the Group:

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

The RBS Group Asset and Liability Management Committee (ALCo) sets and reviews the liquidity risk management framework and limits within the risk appetite set by the Board. ALCo, and by delegation the ALCo Technical Committee, oversees the implementation of liquidity management across the Group.

Regulatory oversight and liquidity framework*

The Group operates across multiple jurisdictions and is subject to a number of regulatory regimes.

The principal regulator, the Prudential Regulation Authority (PRA), has a comprehensive set of liquidity regulations which were revised in 2015 to replace the existing BIPRU 12 regime with the CRD IV liquidity regime in the UK. To comply with the PRA regulatory framework, the RBS Group undertakes the following:

- An annual exercise to complete the Internal Liquidity Adequacy Assessment Process (ILAAP); and
- An annual Liquidity Supervisory Review and Evaluation Process (L-SREP) with the PRA, that involves a comprehensive review of the RBS ILAAP, liquidity policies and risk management framework. This results in the settings of the Individual Liquidity Guidance, which influences the size and overall composition of the liquidity portfolio.

On 1 October 2015 the LCR became the PRA's primary regulatory standard for liquidity, replacing the previous BIPRU 12 regime. LCR is being introduced on a phased basis and UK banks are initially required to maintain a minimum of 80% of LCR, rising to 100% by 1 January 2018.

The Basel Committee on Banking Supervision (BCBS) published its final recommendations for implementation of the NSFR in October 2014, proposing an implementation date of 1 January 2018, by which time banks are expected to meet an NSFR ratio of 100% from this point onwards. The EC has stated that it shall, if appropriate, submit a legislative proposal to the European Parliament by the end of 2016 for implementing the NSFR in the EU. In the meantime, RBS Group uses the definitions from the BCBS guidelines, and its own internal interpretations, to calculate the NSFR.

Measurement, monitoring and contingency planning

In implementing the liquidity risk management framework, a suite of tools are used to monitor, limit and stress test the risks within the balance sheet. The limits control the amount and composition of funding sources, asset and liability mismatches and funding concentrations, in addition to the level of liquidity risk.

Liquidity risks are reviewed at a significant legal entity level daily, and at a business level monthly, with performance reported to ALCos at least monthly. Any breach of internal metric limits will set in motion a series of actions and escalations that could lead to activation of the Contingency Funding Plan (CFP).

The RBS Group maintains a CFP, which forms the basis of analysis and management actions to be undertaken in a liquidity stress. The CFP is linked to stress test results and forms the foundation for liquidity risk limits. The CFP sets out the circumstances under which the plan would be invoked; this includes material worsening of liquidity condition indicators which are reported to senior management daily. It also prescribes a communications plan, roles and responsibilities, as well as potential management actions to take in response to various levels of liquidity stress. On invocation of the CFP, the Contingency Liquidity Team would be convened to identify the likely impact of the stress event and determine the appropriate management response.

Stress testing*

Under the liquidity risk management framework the RBS Group maintains the ILAA, a component of which is an assessment of net stressed liquidity outflows. These liquidity stress tests apply scenario-based behavioural and contractual assumptions to cash inflows and outflows under the worst of three severe stress scenarios, as prescribed by the PRA. These are a market-wide stress, an idiosyncratic stress and a combination of both.

A stress event can occur when either firm-specific or market-wide factors lead to depositors and investors withdrawing or not renewing funding on maturity. This could be caused by many factors including fears over the viability of the firm. Additionally, liquidity stress can be brought on by customers choosing to draw down on loan agreements and facilities.

Simulated liquidity stress testing is performed at least monthly for each business as well as the major operating subsidiaries in order to evaluate the strength of the RBS Group's liquidity position. The stressed outflows are measured over certain time periods which extend from two weeks to three months. The Group is expected to be able to withstand stressed outflows through its own resources (primarily through the use of the liquidity portfolio) without having to resort to extraordinary central bank or governmental support.

Stress tests are designed to examine the impact of a variety of firm-specific and market-wide scenarios on the future adequacy of the liquidity reserves. Stress test scenarios are designed to take into account the RBS Group's experience during the financial crisis, recent market conditions and events. These scenarios can be run at any time in response to the emergence of firm-specific or market-wide risks that could have a material impact on the RBS Group's liquidity position. In the past these have included credit rating changes and political and economic conditions changing in particular countries.

The RBS Group's liquidity risk appetite is measured by reference to the liquidity portfolio as a percentage of net stressed ILAA outflows.

Liquidity portfolio

Liquidity risks are mitigated by a centrally managed liquidity portfolio. The size of the portfolio is determined under the liquidity risk management framework with reference to the RBS Group's liquidity risk appetite.

The majority of the portfolio is centrally managed by RBS Group Treasury, ring-fenced from the CIB trading book, and is the ultimate responsibility of the RBS Group Treasurer. This portfolio is held in the PRA regulated UK Domestic Liquidity Subgroup (UK DoLSub) comprising RBS Group's five licensed deposit taking UK banks: The Royal Bank of Scotland plc, National Westminster Bank Plc, Ulster Bank Limited, Coutts & Co and Adam & Company.

Ulster Bank Ireland Limited, a significant operating subsidiary of RBS plc, holds locally managed portfolios that comply with local regulations that may differ from PRA rules. These portfolios are the responsibility of the local Treasurer who reports to the RBS Group Treasurer.

*unaudited

Liquidity and funding risk continued

The UK DoLSub liquidity portfolio accounted for 97% of the total liquidity portfolio, this portion is available to meet liquidity needs as they arise across the Group. The remaining liquidity reserves are held within non-UK bank subsidiaries, the majority of this portion (3%) is restricted by regulatory requirements and assumed to only be available for use locally.

Separately from the liquidity portfolio, the Group holds high quality assets to meet payment systems collateral requirements; these are managed by RBS Group Treasury but are not freely available to other areas of the Group.

The Group categorises its liquidity portfolio, including its locally managed liquidity portfolios, into primary and secondary liquid assets.

- Primary liquid assets such as cash and balances at central banks, treasury bills and other high quality government and US agency bonds.
- Secondary liquid assets that are eligible as collateral for local central bank liquidity facilities, but do not meet the core local regulatory definition. These assets include own-issued securitisations or whole loans that are retained on balance sheet and pre-positioned with a central bank so that they may be converted into additional sources of liquidity at very short notice.

The composition of the liquidity portfolio is subject to internal policies and limits over quality of counterparty, maturity mix and currency mix. The liquidity value of the portfolio is determined with reference to current market prices and the haircuts necessary to generate cash from the asset.

Liquidity risk

Liquidity portfolio

The table below shows the Group's liquidity portfolio by product, liquidity value and by carrying value. Liquidity value is lower than carrying value as it is stated after discounts applied by the Bank of England and other central banks to instruments, within the secondary liquidity portfolio, eligible for discounting.

	Liquidity value									
	2015						2014			
	31 December			Average			31 December		Average	
	UK DoLSub (1) £m	Other £m	Total £m	UK DoLSub £m	Total £m	Total excluding Citizens £m	Total £m	Total excluding Citizens £m	Total £m	Total excluding Citizens £m
Cash and balances at central banks	67,790	1,432	69,222	67,294	69,442	68,631	67,777	66,409	60,951	59,812
Central and local government bonds										
AAA rated governments	3,201	1,098	4,299	4,069	5,080	5,080	7,898	7,898	5,928	5,906
AA- to AA+ rated governments and US agencies	18,237	787	19,024	11,462	20,934	12,859	16,409	7,128	12,634	5,388
	21,438	1,885	23,323	15,531	26,014	17,939	24,307	15,026	18,562	11,294
Primary liquidity	89,228	3,317	92,545	82,825	95,456	86,570	92,084	81,435	79,513	71,106
Secondary liquidity (2)	59,201	1,369	60,570	54,131	57,654	55,227	56,534	54,244	55,424	52,650
Total liquidity value	148,429	4,686	153,115	136,956	153,110	141,797	148,618	135,679	134,937	123,756
Total carrying value	181,240	4,886	186,126				184,885			

The table below shows the liquidity value of the liquidity portfolio by currency.

Total liquidity portfolio	GBP £m	USD £m	EUR £m	Total £m
2015	109,940	18,781	24,394	153,115
2014 excluding Citizens	93,861	27,617	15,060	136,538
2014 Citizens	—	12,939	—	12,939
2014 total	93,861	40,556	15,060	149,477

Notes:
(1) The PRA regulated UK Domestic Liquidity Subgroup (UK DoLSub) comprising RBS Group's five licensed deposit taking UK banks: The Royal Bank of Scotland plc, National Westminster Bank Plc, Ulster Bank Limited, Coutts & Co and Adam & Company. In addition, certain of RBS Group's significant operating subsidiaries - including Ulster Bank Ireland Limited - hold locally managed portfolios that comply with local regulations that may differ from PRA rules.
(2) Comprises assets eligible for discounting at the Bank of England and other central banks.

Funding risk

The composition of the Group's balance sheet is a function of the broad array of product offerings and diverse markets served by its core businesses. The structural composition of the balance sheet is augmented as needed through active management of both asset and liability portfolios. The objective of these activities is to optimise the liquidity profile, while ensuring adequate coverage of all cash requirements under extreme stress conditions.

The Group's asset and liability types broadly match. Customer deposits provide more funding than customer loans utilise; repurchase agreements are largely covered by reverse repurchase agreements; interbank lending and funding largely nets off and this gap has narrowed over the past 5 years; and derivative assets are largely netted against derivative liabilities.

The Group remains committed to supporting the objectives of the Funding for Lending scheme.

Key funding metrics

The table below summarises the key funding metrics.

	Short-term wholesale funding (1)		Total wholesale funding		Net inter-bank funding (2)		
	Excluding derivative collateral £bn	Including derivative collateral £bn	Excluding derivative collateral £bn	Including derivative collateral £bn	Deposits £bn	Loans (3) £bn	Net inter-bank funding £bn
2015	15.4	35.7	64.4	84.7	7.6	(6.1)	1.5
2014	23.9	48.5	93.8	118.5	15.3	(12.0)	3.3
2014 excluding Citizens	18.7	43.4	86.8	111.5	10.2	(10.3)	(0.1)

Notes:
(1) Short-term wholesale funding is funding with a residual maturity of less than one year.
(2) Excludes derivative cash collateral.
(3) Primarily short-term balances.

Liquidity and funding risk continued

Funding sources

The table below shows the Group's principal funding sources excluding repurchase agreements (repos).

	2015			2014		
By product	Third Party £m	Amounts due to holding company and fellow subsidiaries £m	Total £m	Third Party £m	Amounts due to holding company and fellow subsidiaries £m	Total £m
Deposits by banks						
derivative cash collateral	20,241	—	20,241	24,687	—	24,687
other deposits	7,588	3,999	11,587	10,171	4,208	14,379
	27,829	3,999	31,828	34,858	4,208	39,066
Debt securities in issue						
commercial paper (CP)	—	—	—	58	—	58
certificates of deposit (CDs)	944	—	944	1,178	—	1,178
medium-term notes (MTNs)	16,833	—	16,833	28,402	—	28,402
covered bonds	5,585	—	5,585	7,114	—	7,114
securitisations	2,442	—	2,442	5,244	—	5,244
	25,804	—	25,804	41,996	—	41,996
Subordinated liabilities	8,528	18,502	27,030	10,830	19,639	30,469
Notes issued	34,332	18,502	52,834	52,826	19,639	72,465
Wholesale funding	62,161	22,501	84,662	87,684	23,847	111,531
Customer deposits						
derivative cash collateral	10,360	—	10,360	12,994	—	12,994
other deposits	331,581	5,021	336,602	338,812	5,843	344,655
Total customer deposits	341,941	5,021	346,962	351,806	5,843	357,649
Total funding excluding disposal groups	404,102	27,522	431,624	439,490	29,690	469,180
Disposal group funding	2,837	—	2,837	67,529	—	67,529
Total funding	406,939	27,522	434,461	507,019	29,690	536,709

Repos

The table below analyses the Group's repos by counterparty type.

	2015 £m	2014 £m
Financial institutions		
- central and other banks	10,266	24,784
- other financial institutions	20,130	28,703
Personal and corporate deposits	6,982	8,647
Total excluding disposal groups	37,378	62,134
Disposal groups	—	2,372
Total	37,378	64,506

Reverse repos at 31 December 2015 were £39.9 billion (2014 - £64.7 billion). Fair value of securities received as collateral for reverse repos was £39.8 billion (2014 - £64.7 billion), of which £29.0 billion (2014 - £60.2 billion) had been rehypothecated for the Group's own transactions, in line with normal market practice.

Notes issued

The table below shows the Group's debt securities in issue and subordinated liabilities by residual maturity.

	Debt securities in issue							
2015	CP and CDs £m	MTNs £m	Covered bonds £m	Securitisations £m	Total £m	Subordinated liabilities £m	Total notes in issue £m	Total notes in issue %
Less than 1 year	742	4,996	2,171	4	7,913	239	8,152	16
1-3 years	202	3,785	758	—	4,745	2,288	7,033	13
3-5 years	—	4,307	1,627	—	5,934	92	6,026	11
More than 5 years	—	3,745	1,029	2,438	7,212	5,909	13,121	25
Total excluding disposal groups	944	16,833	5,585	2,442	25,804	8,528	34,332	65
Disposal groups	—	—	—	—	—	—	—	—
Total including disposal groups	944	16,833	5,585	2,442	25,804	8,528	34,332	65
Amounts due from holding company and fellow subsidiaries	—	—	—	—	—	18,502	18,502	35
Total	944	16,833	5,585	2,442	25,804	27,030	52,834	100
2014								
Less than 1 year	1,087	5,712	1,284	10	8,093	2,089	10,182	14
1-3 years	144	8,700	2,229	—	11,073	860	11,933	16
3-5 years	—	4,040	812	3	4,855	1,811	6,666	9
More than 5 years	5	9,950	2,789	5,231	17,975	6,070	24,045	32
Total excluding disposal groups	1,236	28,402	7,114	5,244	41,996	10,830	52,826	71
Disposal groups	665	960	—	—	1,625	226	1,851	3
Total including disposal groups	1,901	29,362	7,114	5,244	43,621	11,056	54,677	74
Amounts due from holding company and fellow subsidiaries	—	—	—	—	—	19,639	19,639	26
Total	1,901	29,362	7,114	5,244	43,621	30,695	74,316	100

Customer loan:deposit ratios and funding surplus

The table below shows third party customer loans, deposits, loan:deposit ratios (LDR) and customer funding surplus.

	Loans (1) £m	Deposits (2) £m	LDR %	Funding surplus £m
2015	306,624	344,746	89	38,122
2014 excluding Citizens	331,628	351,806	94	20,178
2014	391,234	412,356	95	21,122

Notes:
(1) Excludes reverse repurchase agreements and stock borrowing and includes disposal groups.
(2) Excludes repurchase agreements and stock lending and includes disposal groups.

Liquidity and funding risk continued

Encumbrance

The Group evaluates the extent to which assets can be financed in a secured form (encumbrance), but certain asset types lend themselves more readily to encumbrance. The typical characteristics that support encumbrance are an ability to pledge those assets to another counterparty or entity through operation of law without necessarily requiring prior notification, homogeneity, predictable and measurable cash flows, and a consistent and uniform underwriting and collection process. Retail assets including residential mortgages, credit card receivables and personal loans display many of these features.

The Group categorises its assets into three broad groups; assets that are:

- Already encumbered and used to support funding currently in place via own asset securitisations, covered bonds and securities repurchase agreements.
- Positioned with the central bank as part of the Group's contingency funding.
- Not currently encumbered. In this category, the Group has in place an enablement programme which seeks to identify assets which are capable of being encumbered and to identify the actions to facilitate such encumbrance whilst not impacting customer relationships or servicing.

The Group's third party balance sheet encumbrance ratios are set out below.

Encumbrance ratios - third party	2015 %	2014 %	2014 excluding Citizens %
Total	11	13	12
Excluding balances relating to derivative transactions	11	14	13
Excluding balances relating to derivative and securities financing transactions	8	11	10

Balance sheet encumbrance - third party

2015	Encumbered as a result of transactions with counter parties other than central banks: Covered bonds and securitisations(1) £bn	Derivatives £bn	Repos and similar(2) £bn	Total enc assets(3) £bn	Assets encumbered at the central bank and unencumbered assets: Positioned at the central bank(4) £bn	Readily available for enc(5) £bn	Capable of being enc(6) £bn	Cannot be enc(7) £bn	Total unenc assets £bn	Total third party £bn	Balances with holding company and fellow subsidiaries £bn	Total £bn
Cash and balances at central banks	—	—	2.5	2.5	70.3	6.2	—	—	76.5	79.0	—	79.0
Loans and advances												
- banks	1.5	11.0	0.4	12.9	1.5	2.4	0.3	0.1	4.3	17.2	1.6	18.8
- residential mortgages												
- UK	15.2	—	—	15.2	81.3	18.6	8.4	—	108.3	123.5	—	123.5
- Irish	7.4	—	—	7.4	1.2	4.0	—	0.1	5.3	12.7	—	12.7
- credit card	—	—	—	—	—	4.4	0.2	—	4.6	4.6	—	4.6
- personal loans	—	—	—	—	—	6.0	3.5	—	9.5	9.5	—	9.5
- other	0.5	17.2	0.4	18.1	8.3	8.8	97.7	21.8	136.6	154.7	1.2	155.9
Reverse repos	—	—	—	—	—	—	—	39.8	39.8	39.8	—	39.8
Debt securities	—	2.9	31.8	34.7	20.9	24.3	0.1	—	45.3	80.0	—	80.0
Equity shares	—	—	—	—	—	0.7	0.1	0.3	1.1	1.1	—	1.1
Settlement balances	—	—	—	—	—	—	—	4.0	4.0	4.0	0.1	4.1
Derivatives	—	—	—	—	—	—	—	261.8	261.8	261.8	1.3	263.1
Intangible assets	—	—	—	—	—	—	—	6.5	6.5	6.5	—	6.5
PPE	—	—	0.3	0.3	—	—	3.1	1.1	4.2	4.5	—	4.5
Deferred tax	—	—	—	—	—	—	—	2.6	2.6	2.6	—	2.6
Other assets	—	—	—	—	—	—	—	3.0	3.0	3.0	—	3.0
Total before disposal groups	24.6	31.1	35.4	91.1	183.5	75.4	113.4	341.1	713.4	804.5	4.2	808.7
Disposal groups	—	—	—	—	—	0.8	2.0	0.7	3.5	3.5	—	3.5
Total	24.6	31.1	35.4	91.1	183.5	76.2	115.4	341.8	716.9	808.0	4.2	812.2
Securities retained					2.9							
Total liquidity portfolio					186.4							
Liabilities secured												
Intra-Group - secondary liquidity	(3.7)	—	—	(3.7)								
Intra-Group - other	(6.2)	—	—	(6.2)								
Third-party (8)	(8.0)	(31.1)	(39.6)	(78.7)								
	(17.9)	(31.1)	(39.6)	(88.6)								

For the notes to this table refer to the following page.

Liquidity and funding risk continued

Balance sheet encumbrance - third party

2014*	Encumbered as a result of transactions with counter parties other than central banks: Covered bonds and securitisations(1) £bn	Derivatives £bn	Repos and similar(2) £bn	Total enc assets(3) £bn	Assets encumbered at the central bank and unencumbered assets: Positioned at the central bank(4) £bn	Readily available for enc(5) £bn	Capable of being enc(6) £bn	Cannot be enc(7) £bn	Total unenc assets £bn	Total third party £bn	Balances with holding company and fellow subsidiaries £bn	Total £bn
Cash and balances at central banks	—	—	2.4	2.4	66.1	5.5	—	—	71.6	74.0	—	74.0
Loans and advances												
- banks	4.9	11.3	0.5	16.7	0.4	0.7	3.8	—	4.9	21.6	2.3	23.9
- residential mortgages												
- UK	25.4	—	—	25.4	69.9	10.2	7.7	0.1	87.9	113.3	—	113.3
- Irish	8.6	—	—	8.6	0.9	4.3	—	0.1	5.3	13.9	—	13.9
- credit card	2.7	—	—	2.7	—	2.3	0.2	—	2.5	5.2	—	5.2
- personal loans	—	—	—	—	—	6.4	2.9	—	9.3	9.3	—	9.3
- other	5.6	21.7	0.5	27.8	7.9	9.6	106.3	38.4	162.2	190.0	1.3	191.3
Reverse repos	—	—	—	—	—	—	—	64.7	64.7	64.7	—	64.7
Debt securities	—	5.6	26.5	32.1	13.2	38.7	0.3	—	52.2	84.3	—	84.3
Equity shares	—	0.3	2.6	2.9	—	2.1	0.2	—	2.3	5.2	—	5.2
Settlement balances	—	—	—	—	—	—	—	4.7	4.7	4.7	—	4.7
Derivatives	—	—	—	—	—	—	—	351.9	351.9	351.9	2.7	354.6
Intangible assets	—	—	—	—	—	—	—	7.8	7.8	7.8	—	7.8
PPE	—	—	0.4	0.4	—	—	3.7	2.0	5.7	6.1	—	6.1
Deferred tax	—	—	—	—	—	—	—	1.8	1.8	1.8	—	1.8
Other assets	—	—	—	—	—	—	—	4.1	4.1	4.1	0.2	4.3
Total before disposal groups	47.2	38.9	32.9	119.0	158.4	79.8	125.1	475.6	838.9	957.9	6.5	964.4
Disposal groups	—	0.3	16.4	16.7	13.8	8.5	1.7	40.3	64.3	81.0	—	81.0
Total	47.2	39.2	49.3	135.7	172.2	88.3	126.8	515.9	903.2	1,038.9	6.5	1,045.4
Securities retained					12.7							
Total liquidity portfolio					184.9							
Liabilities secured												
Intra-Group - secondary liquidity	(13.1)	—	—	(13.1)								
Intra-Group - other	(11.6)	—	—	(11.6)								
Third-party (8)	(12.3)	(39.2)	(64.6)	(116.1)								
Total before disposal groups	(37.0)	(39.2)	(64.6)	(140.8)								
Disposal groups	—	—	(10.4)	(10.4)								
Total	(37.0)	(39.2)	(75.0)	(151.2)								

*Restated - refer to page 148 for further details.

Notes:
(1) Covered bonds and securitisations include securitisations, conduits and covered bonds.
(2) Repos and other secured deposits, cash, coin and nostro balance held with the Bank of England as collateral against deposits and notes in circulation are included here rather than within those positioned at the central bank as they are part of normal banking operations.
(3) Total assets encumbered (enc) as a result of transactions with counterparties other than central banks are those that have been pledged to provide security for the liability shown above and are therefore not available to secure funding or to meet other collateral needs.
(4) Assets positioned at the central bank relates to the Group's liquidity portfolio and comprises cash balances at central banks, high quality debt securities and loans that have been pre-positioned with central banks. In addition, the liquidity portfolio includes securitisations of own assets which has reduced over the years and has been replaced by loans.
(5) Readily available for encumbrance (enc): including assets that have been enabled for use with central banks but not positioned; and unencumbered debt securities.
(6) Other assets that are capable of being encumbered (enc) are those assets on the balance sheet that are available for funding and collateral purposes but are not readily realisable in their current form. These assets include loans that could be prepositioned with central banks but have not been subject to internal and external documentation review and diligence work.
(7) Cannot be encumbered (enc) includes:
(a) Derivatives, reverse repurchase agreements and trading related settlement balances.
(b) Non-financial assets such as intangibles, prepayments and deferred tax.
(c) Loans that cannot be pre-positioned with central banks based on criteria set by the central banks, including those relating to date of origination and level of documentation.
(d) Non-recourse invoice financing balances and certain shipping loans whose terms and structure prohibit their use as collateral.
(8) In accordance with market practice, the Group employs securities recognised on the balance sheet, and securities received under reverse repo transactions as collateral for repos. Secured derivative liabilities reflect net positions that are collateralised by balance sheet assets.

Business risk*

Definition

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

The Group could make inappropriate business or strategic choices if it fails to adequately assess the current and prospective operating environment. It may not be able to execute its chosen strategy in line with its budget if there are material changes to its internal or external operating environment.

All the disclosures in this section are unaudited.

Sources of risk

Business risk arises as a result of the Group's exposure to the macro-environment, to the competitive environment, and to technological changes. In addition, internal factors such as volatility in sales volumes, and input costs, and other operational risks such as the Group's ability to assess the business operating environment, or to execute its chosen strategy, contribute to business risk.

Governance

The RBS Group Board has ultimate responsibility for business risk and for approving strategic plans, initiatives and changes to strategic direction. Refer to the Risk governance section on page 30.

The RBS Group's strategic planning process is managed by Strategy and Corporate Development. The Risk and Finance functions are key contributors to strategic planning. As part of the process, each customer business develops a strategic plan within a framework set by the RBS Group's senior management. The strategic plans are consolidated at RBS Group-wide level, and reviewed and assessed against risk appetite by the RBS Group's Chief Executive, the Chief Financial Officer and the Director of Strategy and Corporate Finance before presentation to, and approval by, the Board.

Responsibility for the day-to-day management of business risk lies primarily with the franchises with oversight by the Finance function. The franchises are responsible for delivery of their business plans and the management of such factors as pricing, sales volumes, marketing expenditure and other factors that can introduce volatility into earnings.

Risk assessment, controls and assurance

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

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

The following aspects of the strategic planning process also control business risk:

- The Top Risks process which aims to identify early, monitor closely and avoid or otherwise manage effectively strategic risks that have the highest likelihood of impacting strategic plans; and
- At the end of the strategic planning process sensitivity analysis is undertaken on the consolidated budget to assess the robustness of the plan and compliance with strategic risk objectives, including under a variety of stressed conditions.

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

- Organisational capabilities;
- Organisational resources;
- Organisational commitment; and
- Stakeholder requirements, including customers, regulators, employees, and investors.

Business risk is also controlled via the monthly performance review processes which include financial reviews carried out by the Finance Function via the franchise Finance Directors and Financial Planning & Analysis. These reviews are carried out to understand emerging trends, issues and, where there are adverse variations from plans, enable management to take appropriate actions. A wide variety of financial, risk, customer and market metrics are monitored to assess business performance and hence the effectiveness of chosen strategies. Deviations from plan are analysed to determine drivers which could be strategic, environmental or management-related. The monthly performance review process also includes the provision of monthly reports to the Executive Committees and the Board.

In addition, business performance reviews are carried out on a quarterly basis to discuss detailed business issues and agree action plans. These are led by franchise Chief Executive Officers and Finance Directors, with the RBS Group's Chief Executive, Chief Financial Officer, Chief Risk Officer and other stakeholders in attendance.

Finally, business risk is controlled through the adoption of policy standards that inform the approach to strategy development and business planning. Examples include the policy standards on Corporate Governance, Business Commitment Approval Process, Acquisitions & Disposals, Capital Management and Political Legislative & Regulatory Environment.

*unaudited

Business risk* continued

Risk appetite

Refer to the Risk appetite section on page 35.

Risk identification and monitoring

Business risk is identified and managed at the product and transaction level. Estimated revenue, costs and capital, including the potential range of outcomes, are key considerations in the design of any new product or investment decision. All policies that ultimately seek to manage and control financial impact at the product and transaction level are therefore relevant to business risk management, including policies on conduct, funding and investment spending.

Business risk is reported, assessed and challenged at every governance level within the organisation. Each franchise monitors its financial performance relative to plans and reports this on a regular basis to the Finance Directors of each franchise. The monthly and quarterly performance review processes described above, as well as the Top Risks process are also all central to the identification and monitoring of business risk.

Business risk is reviewed and assessed through the planning cycles. Financial plans are developed on a bottom-up basis and refined under expected and potential scenarios reflecting expectations of the external environment and strategic priorities. These scenarios are tested against a range of sensitivities and stresses to identify the key risk drivers behind any potential volatility, together with management actions to address and manage them.

Risk mitigation

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

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

A major part of the Top Risks process is to ensure that all appropriate action is taken to mitigate the most material risks to strategic objectives.

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

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

*unaudited

Risk measurement

A wide variety of financial, risk, customer and market metrics are used to monitor business performance and thus, inter alia, the effectiveness of chosen strategies. Any deviations from the expected values are analysed to determine drivers which could be strategic, environmental or management. Example metrics include: customer attrition, deposit balances, revenues, impairments or loan losses, profitability and risk-weighted returns.

The stress test outcomes form a core part of the assessment of earnings and capital adequacy risk appetite and are approved by the Board. The measurement of change in profit and loss of the franchises under stress thereby acts as a measure of business risk. Franchises also conduct their own bottom-up stress testing exercises to assess the financial performance of their businesses under stress.

Reputational risk*

Definition

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

All the disclosures in this section are unaudited.

Sources of risk

Reputational risk can arise from the conduct of either the RBS Group as a whole or that of the individuals it employs; from the activities of customers and the countries in which they operate; from the products the RBS Group offers and the transactions it supports; and from its operations and infrastructure.

Governance

Reputational risk is of significant importance and is controlled by a governance framework, with Board-level oversight reinforced by a Reputational Risk Policy.

Reputational risk appetite is agreed at RBS Group-wide level by the Executive Risk Forum (ERF) and cascaded to business franchises and functions.

The Sustainable Banking Committee is responsible for overseeing how the RBS Group manages its reputation and delivers its commitments on trust, advocacy, and customer service.

The Board's oversight of reputational issues is supported by the senior RBS Group-wide Reputational Risk Forum (RRF), which opines on cases that represent a material reputational risk to the whole organisation. The RRF, which has delegated authority from the ERF, also acts as a central forum to approve sector or theme-specific reputational risk appetite positions (including Environmental, Social & Ethical risk positions) following review at business franchise risk committees.

Risk appetite

Refer to the Risk appetite section on page 35.

Risk monitoring and measurement

Emerging reputational issues are identified by business franchises and functions with the Sustainability Services and Enterprise Wide Risk teams focusing on new and emerging sustainability and strategic risks respectively. The Risk Management Monthly Report, provided to the Executive Risk Forum and the Board Risk Committee (BRC), may also discuss reputational risks facing the RBS Group, and the annual Sustainability Report covers progress on sustainability principles.

Management information on customers, transactions, products or issues that have been escalated to relevant reputational risk approving authorities and forums is captured by each business franchise with select cases being reviewed by senior risk committees within the businesses. A summary of material reputational risk issues discussed at the senior RBS Group-wide Reputational Risk Forum is also provided in the Risk Management Monthly Report.

ESE ratings of customers and transactions are captured and analysed centrally by the Reputational and ESE Risk Team and reported externally in the annual Sustainability Report.

Risk mitigation

Reputational risk is mitigated through governance frameworks and training of staff to ensure early identification, assessment and escalation of cases with potential reputational risk, if appropriate. This includes creating appropriate fora, for example reputational risk committees or individual reputational risk approvers.

Also important is the setting of clear reputational risk appetite criteria, ensuring higher risk cases are escalated for informed debate and senior-level approval. Effective communication channels and incident response planning also ensure that cases resulting in reputational impact are appropriately managed, for example by declining or exiting business or by ensuring incident management plans are implemented to manage the impact of negative media coverage.

Conduct and regulatory risk*

Definition

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

All the disclosures in this section are unaudited.

*unaudited

Sources of risk

Conduct and regulatory risk exists across all stages of the RBS Group's relationships with its customers, from the development of its business strategies, through governance arrangements, to post-sales processes. Activities through which conduct risk may arise are diverse and include product design, marketing and sales, complaint handling, staff training, and handling of confidential and non-public price sensitive information. Conduct risk also exists if the RBS Group does not take effective action to prevent fraud, bribery and money laundering. Regulatory risk arises from the regulatory, business or operating environment and from the RBS Group's response to it.

As set out in the Litigation, Investigations and Reviews section, the RBS Group and certain members of it are party to legal proceedings and are subject to investigation and other regulatory action in the UK, the US and other jurisdictions.

Governance

RBS Group Conduct & Regulatory Affairs (C&RA) is responsible for defining appropriate standards of conduct, and for driving adherence to them, for designing the framework for managing conduct and regulatory risk, and for overseeing remediation activity. It also provides appropriate controls, challenge and oversight to ensure good customer outcomes. In so doing, C&RA acts as a second line of defence control function.

Key elements of the governance structure are set out below:

- The C&RA Executive Committee considers emerging issues material to C&RA's strategy, and implements Board and Executive Committee risk management policy decisions;
- The Financial Crime Accountable Executive Committee (accountable to the Executive Risk Forum) ensures that the customer businesses and the Services function fulfil strategic objectives by identifying and managing their financial crime risks effectively; and
- The Mandatory Change Advisory Committee (MCAC), reports to the Bank-Wide Investment Committee, and comprises representatives of the customer businesses and functions. The MCAC acts as the 'reception committee' for reviewing externally mandated changes that may affect the RBS Group and recommending appropriate responses, including the timely mobilisation of change implementation activities. In doing so, it agrees business or function owners of individual risks; and commissions and reviews impact assessments from customer businesses and functions.

Controls and assurance

Under the RBS Group Policy Framework, C&RA owns 23 conduct risk policies. Each policy is designed to provide both high-level direction and RBS Group-wide requirements. The policies are designed to ensure the RBS Group meets its regulatory obligations, and to provide the necessary clarity for staff on their conduct obligations.

C&RA's Regulatory Affairs department separately oversees the regulatory changes, interactions with regulators and regulatory approvals for individuals.

Conduct and regulatory risk* continued

Assurance and monitoring activities are essential to help measure the extent to which the RBS Group manages its delivery of specific customer outcomes.

Risk assessments are used to identify material conduct risks and key controls across all business areas. The risk assessment process is designed to confirm that risks are effectively managed and prioritised and that controls are tested.

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

Risk appetite

Work to refine and embed the risk appetite framework and associated control processes continued in 2015. The risk appetite statements set the minimum standards which the franchises augment with specific conduct risks inherent in their business model. The franchises undertake an annual self-assessment of the inherent and residual conduct risks against the risk appetite statements.

Risk monitoring and measurement

C&RA works closely with the customer-facing businesses to assess business models, strategy and products and influence better outcomes for customers. The RBS Group's senior boards and committees receive updates on conduct risk exposures and action plans through monthly C&RA-initiated reporting. The reporting is intended to be focused, forward-looking and action-oriented.

C&RA provides appropriate reporting of all material regulatory reviews and other regulatory developments worldwide to the appropriate RBS Group-wide committees, including the Board, the Group Audit Committee and the BRC.

An annual Money Laundering Reporting Officer's Report is submitted to the Board and the FCA. Covering the operation and effectiveness of the systems and controls in place to comply with Anti-Money Laundering (AML) law and regulation, it also describes the RBS Group's AML framework. In addition, it covers the systems and controls in place to prevent the financing of terrorism and to ensure compliance with sanctions as well as embargoes and export controls imposed by the UN, governments and other supranational bodies.

The Group Audit Committee is provided with an annual Whistleblowing Update Report. It details cases by internal reporting categories based on the Public Interest Disclosure Act (1998); identifies underlying causal and subject trends; and highlights the outcome of investigations and actions taken.

C&RA is working with each business to enhance the management information linked to their risk appetite statements. This is required to ensure appropriate customer outcomes are delivered, and that the management information is compliant with the Basel Committee on Banking Supervision principles for effective risk data aggregation and risk reporting.

*unaudited

Risk mitigation

C&RA communicates information on regulatory developments, and follow-ups with regulators, to customer-facing businesses and functions, helping them identify and execute any required mitigating changes to strategy or business models.

Early identification and effective management of changes in legislation and regulation, are critical to the successful mitigation of conduct and regulatory risk. All regulatory and compliance changes are managed to ensure timely compliance readiness. Those changes assessed as having a 'High' or 'Medium-High' impact are managed especially closely, with the aim of mitigating the impact through, for instance, changes to strategy or business activities, or external engagement.

Operational risk*

Definition

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

Operational risks may have a direct customer or reputational impact (for example, a major IT systems failure or fraudulent activity) or both. Operational risk failures may also have a link with conduct risk failures.

All the disclosures in this section are unaudited.

Sources of risk

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

Cyber risk

Cyber attacks are increasing in frequency and severity across the industry and their threat to the security of the RBS Group's information from continues to be closely monitored. During 2015, the RBS Group participated in industry-wide cyber attack simulations in order to help test and develop defence planning. To mitigate the risks, a large-scale programme to improve user access controls is in progress, along with a number of other actions, including a reduction in the number of external websites, enhancement of protection against malware, and the implementation of a staff education programme on information protection.

Risk governance

A strong operational risk management function is vital to support the RBS Group's ambitions. Better management of operational risk directly supports the strategic risk objective of improving stakeholder confidence and is vital for stability and reputational integrity.

The operational risk function, an independent second line of defence, plays a leadership role and seeks to achieve a robust operational risk management framework and culture across the RBS Group. The Global Head of Operational Risk reports to the Chief Risk Officer.

The operational risk function is responsible for the design, development, delivery and continuous improvement of the ORMF. The Operational Risk Policy is incorporated in the RBS Group Policy Framework and provides direction for the consistent identification, assessment, management, monitoring and reporting of operational risk. Through a network of oversight teams, the function undertakes second line of defence oversight and challenge to ensure the integrity of the ORMF, and manages the overall operational risk profile against risk appetite.

The Operational Risk Executive Committee (OREC), which is a sub-committee of the Executive Risk Forum (ERF), acts on all operational risk matters. This includes reviewing the operational risk exposure against risk appetite; identifying and assessing material operational risks, encompassing both current and emerging material risks; reviewing and monitoring the operational risk profile; and reviewing and approving material policy changes.

Controls and assurance

The Control Environment Certification (CEC) process is a half-yearly self-assessment of the adequacy and effectiveness of the RBS Group's internal control environment. This covers material risks and the key controls that underpin them, including financial, operational and compliance controls, as well as the supporting risk management frameworks.

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

The CEC helps to ensure compliance with the RBS Group Policy Framework, Sarbanes-Oxley 404 requirements concerning internal control over financial reporting (as referenced in the Compliance report section), and the requirements of the UK Corporate Governance Code.

Risk appetite

The operational risk appetite framework is place to manage the risk to an acceptable level in line with stated risk appetite. Risk appetite provides the RBS Group with a clear understanding of its acceptable levels of risk in relation to its strategic objectives and wider obligations.

This has led to the development of a number of risk appetite statements covering the RBS Group's most material operational risks. These risks were identified due to their significance and they are regularly reported to the OREC, the ERF and the BRC. Work has commenced to cascade these statements to each business. The statements are monitored and reported at business risk committees.

Above these sits an RBS Group-level operational risk appetite statement which encompasses the full range of operational risks and drives the strategic risk measurement of stakeholder confidence. This is reviewed annually by the ERF. The statement is supported by three simple measures: (i) the relationship between operational risk losses and the RBS Group's gross income; (ii) metrics covering control environment performance; and (iii) the requirements for the material RBS Group-wide operational risks to be managed within risk appetite.

Risk identification and assessment

Risk and control assessments are used to identify and assess material operational and conduct risks and key controls across all business areas. To support identification of risk concentrations, all risks and controls are mapped to the risk directory. Risk assessments are refreshed at least annually to ensure they remain relevant and capture any emerging risks.

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

During 2015, an enhanced end-to-end risk assessment methodology was designed, which is now being implemented across the RBS Group. This approach enhances the understanding of the risk profile of the RBS Group's key products and services, and it will be used to identify and quantify the most material risks. Subject matter experts and key stakeholders are engaged from across the RBS Group to support management decision-making in line with the RBS Group's financial and non-financial appetite statement.

The New Product Risk Assessment process aims to ensure that the risks represented by new products (and material variations to existing products) are identified and assessed before launch. There is now a requirement to demonstrate that all products provide fair outcomes to customers. Ongoing enhancements to improve the risk rating of new and significant changes to products as well as increasing the focus on customers were introduced during 2015.

*unaudited

Operational risk* continued

Risk mitigation

Risks are mitigated through the application of key preventative and detective controls as an integral step in risk assessment methodology, to enable a determination of the residual risk. Control owners are accountable for the design, execution, performance and maintenance of key controls.

These key controls are regularly assessed for adequacy and tested for effectiveness. The control testing results are monitored and, where a material change in performance is identified, it results in a re-evaluation of the associated risk. During 2015, work continued on enhancing management information reporting, driving consistency and more focused actions to mitigate risk.

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

Risk monitoring

Monitoring and reporting are part of the RBS Group's operational risk management processes, which aim to ensure that risks and issues are identified, considered by senior executives, and managed effectively.

The most material operational risks and their position relevant to risk appetite are regularly reviewed at the OREC, along with any emerging risks and the actions taken to mitigate them. These are also reported to the BRC and the ERF. Exposures specific to each business are communicated through monthly risk and control reports that are discussed at business risk committees.

Risk measurement

The RBS Group uses the standardised approach to calculate its operational risk capital requirement. This is based upon multiplying three years' average historical gross income by co-efficients set by the regulator based on type of income.

As part of the wider Internal Capital Adequacy Assessment Process (ICAAP) an operational risk economic capital model is used as a key capital benchmark. The model utilises loss data and scenario analysis inputs from the operational risk framework to provide a risk sensitive view of the RBS Group's operational risk capital requirement.

Scenario analysis is used to assess the potential impact of extreme but plausible operational risks. It provides a forward-looking basis for evaluating and managing operational risk exposures.

Capital

Pillar 1 capital requirements for operational risk are set out in the Capital management section - Measurement - capital, RWAs and leverage.

Event and loss data management

The event and loss data management process ensures the capture and recording of operational risk loss events that meet defined criteria. The loss data is used for regulatory and industry reporting and is included in the capital modelling, for the calculation of the regulatory capital for operational risk.

*unaudited

Event and loss data management

The event and loss data management process ensures the capture and recording of operational risk loss events that meet defined criteria. The loss data is used for regulatory and industry reporting and is included in the capital modelling, for the calculation of the regulatory capital for operational risk.

The most serious events are escalated in a simple, standardised process to all senior management, by way of the Group Notifiable Event Process. All losses and recoveries associated with an operational risk event are reported against their financial accounting date. A single event can result in multiple losses (or recoveries) that may take time to crystallise. Losses and recoveries with a financial accounting date in 2015 may relate to events that occurred, or were identified in, prior years.

Pension risk*

Definition

Pension obligation risk is the risk to the RBS Group caused by its contractual or other liabilities to or with respect to a pension scheme (whether established for its employees or those of a related company or otherwise). It also means the risk that the RBS Group will make payments or other contributions to or with respect to a pension scheme because of a moral obligation or because it considers that it needs to do so for some other reason.

All the disclosures in this section are unaudited.

Sources of risk

The Group has exposure to pension risk through its defined benefit schemes worldwide. The largest scheme, which represents around 90% of the Group's pension liabilities, is the Royal Bank of Scotland Group Pension Fund (Main scheme). The three other biggest schemes are the Ulster Bank Pension Scheme (Republic of Ireland), the Ulster Bank Pension Scheme and the Royal Bank of Scotland International Pension Trust. The Main scheme is the principal source of pension risk.

Pension scheme liabilities vary with changes in long-term interest rates and inflation as well as with pensionable salaries, the longevity of scheme members and legislation. Meanwhile, pension scheme assets vary with changes in interest rates, inflation expectations, credit spreads, exchange rates and equity and property prices. The Group is exposed to the risk that the schemes' assets together with future returns and any additional future contributions are insufficient to meet liabilities as they fall due. In such circumstances, it could be obliged (or might choose) to make additional contributions to the schemes or be required to hold additional capital to mitigate this risk.

Key developments in 2015

A payment of £650 million was made to the Main scheme in 2015 in line with the current Schedule of Contributions, in addition to the regular annual contribution of around £270 million for ongoing accrual of benefits and the expenses of running the scheme. Following developments in pension accounting and reporting during 2015, RBS Group revised its policy for determining whether or not it has an unconditional right to a refund of any surpluses in its employee pension funds and also revised prior periods (refer to page 148 - Accounting policies and page 168 Note 4, Pensions, for more details).

The incremental impact of this, combined with the one-off accelerated payment expected of £4.2 billion to be made in 2016, is anticipated to improve RBS Group's risk profile, capital planning, and resilience through the period to 2019. Subject to PRA approval, the adverse core capital impact resulting from the accounting policy change and the accelerated payment is expected to be partially offset by a reduction in core capital requirements. Any such core capital offsets are likely to occur at the earliest from 1 January 2017, but they will depend on the PRA's assessment of CET1 capital position at that time.

Governance

The Main scheme operates under a trust deed. The corporate trustee, RBS Pension Trustee Limited, is a wholly owned subsidiary of The Royal Bank of Scotland plc. The trustee board currently comprises six directors selected by the RBS Group and four directors nominated by members. The trustee is supported by RBS Investment Executive Ltd (RIEL), a team which specialises in pension investment strategy.

The Pension Risk Committee (PRC) chaired by the RBS Group Treasurer, acts as a sub-committee of the RBS Asset and Liability Committee (ALCo) and formulates the RBS Group's view of pension risk. The PRC considers mechanisms that could potentially be used for managing risk within the pension schemes as well as financial strategy and employee welfare implications, and also reviews actuarial assumptions from a sponsor perspective as appropriate. The PRC is a key component of the RBS Group's approach to pension risk where risk management, asset strategy and financing issues are reviewed and monitored on behalf of the RBS Group. The PRC also serves as a formal link between the RBS Group, RIEL and the trustee.

For further information on Risk governance, refer to page 30.

Risk appetite

Investment policy for the schemes is defined by the trustee with input from RIEL and other specialist advisers employed by the trustee. While the trustee is responsible for the management of the scheme assets, it consults with the RBS Group on material changes to the Main scheme's risk appetite and investment policy.

The RBS Group maintains an independent view of the risk inherent in pension funds, with an associated risk appetite, and has defined limits against which risk is measured. In addition to the scrutiny provided by the PRC, the RBS Group also achieves this through regular pension risk monitoring and reporting to the Board, the Executive Committee and the BRC on the material pension schemes that the RBS Group has an obligation to support.

Risk mitigation

The trustee has taken measures to mitigate inflation and interest rate risks both by investing in suitable financial assets and by entering into inflation and interest rate swaps. The Main scheme also uses derivatives to manage the allocation of the portfolio to different asset classes and to manage risk within asset classes. The assets of the Main scheme, which represented 90% of RBS Group's pension plan assets at 31 December 2015, are invested in a diversified portfolio of quoted and private equity, government and corporate fixed interest and index-linked bonds, property and other alternative assets.

Risk monitoring and measurement

Pension risk reporting is submitted quarterly to the RBS Group in the RBS Group Risk Monthly Management Report. The report includes a measurement of the overall deficit or surplus position based on the latest data, estimated capital requirements and an assessment of the associated assets and liabilities.

The RBS Group also undertakes a number of stress tests and scenario analyses on its material defined benefit pension schemes each year as part of its risk measurement framework. These stress tests are also used to satisfy the requests of regulatory bodies such as the Bank of England. The stress testing framework includes the production of the pension risk ICAAP as well as additional stress tests for a number of internal management purposes.

Pension stress tests take the form of both stochastic and deterministic stresses over time horizons ranging from instantaneous to five years in duration. They are designed to examine the behaviour of the pension schemes' assets and liabilities under a range of financial and demographic shocks. The results of the stress tests and their consequential impact on the RBS Group's balance sheet, income statement and capital position are incorporated into the overall RBS Group-wide stress test results.

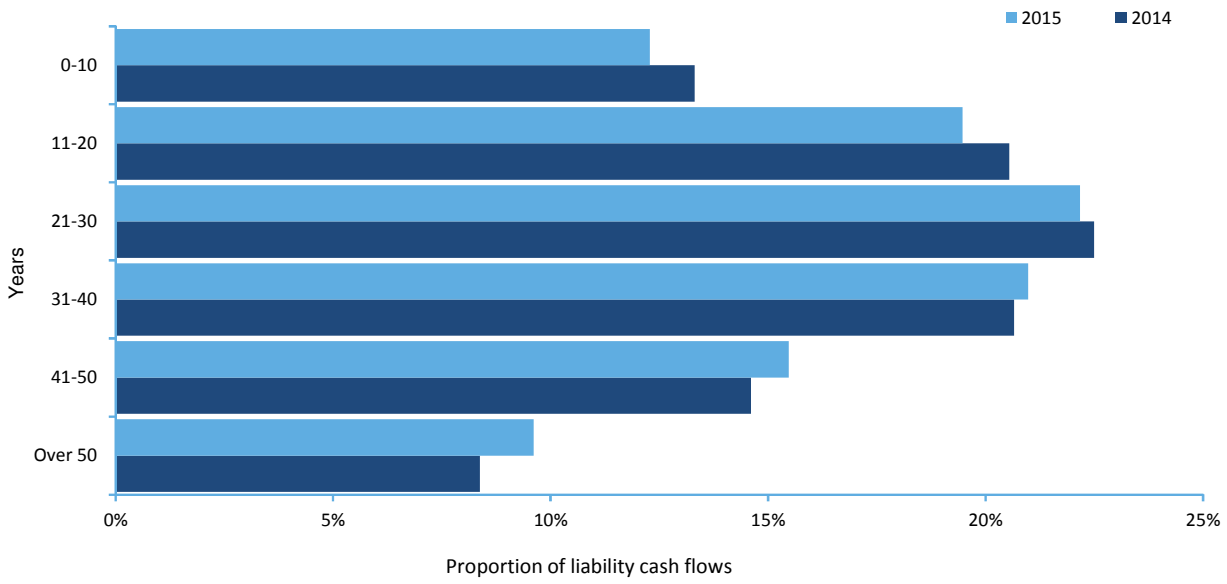
*unaudited

Pension risk* continued

The table below shows the sensitivity of the Main scheme's assets and liabilities (measured according to IAS 19 'Employee Benefits') to changes in interest rates and equity values at the year end, taking account of the current asset allocation and hedging arrangements. Asset sensitivity to changes in nominal yields increased over the year as swap yields fell at longer durations and the Main scheme increased its interest rate hedging ratio.

2015	Change in value of assets £m	Change in value of liabilities £m	Change in net pension obligations £m
Fall in nominal swap yields of 0.25% at all durations with no change in credit spreads or real swap yields	874	363	511
Fall in real swap yields of 0.25% at all durations with no change in credit spreads or nominal swap yields	1,029	1,104	(75)
Fall in credit spreads of 0.25% at all durations with no change in nominal or real swap yields	70	1,526	(1,456)
Fall in equity values of 10%	(667)	—	(667)
2014			
Fall in nominal swap yields of 0.25% at all durations with no change in credit spreads or real swap yields	447	413	34
Fall in real swap yields of 0.25% at all durations with no change in credit spreads or nominal swap yields	932	1,159	(227)
Fall in credit spreads of 0.25% at all durations with no change in nominal or real swap yields	65	1,581	(1,516)
Fall in equity values of 10%	(771)	—	(771)

The chart below shows the pension liability cash flow profile, allowing for expected indexation of future payments. The majority of expected cash flows (77%) are anticipated within the next 40 years. The profile will vary depending on the assumptions made regarding inflation expectations and mortality.



*unaudited

Credit risk: management basis

Definition

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

The following disclosures in this section are audited:

- Risk assessment and monitoring
- Wholesale credit risk management
  - Risk mitigation;
  - Problem debt management - Forbearance
  - Key credit portfolios - commercial real estate LTV distribution
- Personal credit risk management
  - Problem debt management - Forbearance
  - Overview of personal portfolios - Forbearance; and LTV distribution
- Country risk - Summary of country exposures

Sources of credit risk*

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

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

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

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

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

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

Overview and key developments

Credit quality and impairment - The portfolio reduced due to the strategic disposal of Citizens and Capital Resolution assets. Improvement in asset quality was evidenced by a reduction in the number of customers showing financial stress, the number of customers in default and a release of provisions. This was achieved against a backdrop of supportive economic conditions in the Group's key markets.

UK personal lending - The Group's Personal portfolio grew in mortgage lending while underwriting standards remained unchanged. This reflected improving economic conditions as well as the continued low interest rate environment.

Natural Resources - The Oil & Gas sector was affected by the large drop in oil price with prices remaining volatile. Exposures to the Oil & Gas sector materially reduced during 2015. Asset quality remains strong with the majority of the portfolio remaining investment grade. However, changing market conditions resulted in a limited number of customers experiencing financial stress during the year. The Mining & Metals sector was affected by the global market imbalance, prompted by a slowdown in demand - especially from China - and oversupply of the key metal commodities following a legacy of heavy investment in new production capacity. There was a particular focus on mining, which is most vulnerable in these circumstances. Market conditions remained challenging, especially for customers with high financial or operational leverage. Exposure to the Mining & Metals sector reduced materially during 2015. The sector was subject to heightened credit monitoring and ongoing risk appetite review. For further information, refer to the Key credit portfolios section on page 82.

Automotive - As a result of market events, heightened credit monitoring and an ongoing risk appetite review were introduced for this sector with proactive management of direct and indirect exposures. However, no deterioration of asset quality was observed. For further information, refer to the Key credit portfolios section on page 86.

Emerging markets - Exposure decreased as the Group continued to withdraw from non-strategic countries. The reduction in exposure to China during 2015 reflected corporate loan sales and reductions in bank cash collateral due to a decrease in volumes of foreign exchange trade. For further information, refer to the Country risk section on page 96.

Credit risk management function*

Governance

The activities of the Group's credit risk management function, which is led by the Group Chief Credit Officer (GCCO), include:

- approving credit for customers;
- ensuring that credit risk is within the risk appetite set by the Board;
- managing concentration risk and credit risk control frameworks;
- developing and ensuring compliance with credit risk policies; and
- conducting Group-wide assessments of provision adequacy.

*unaudited

Credit risk: management basis continued

The key elements of the credit risk management function are set out below.

Leadership	GCCO	The GCCO has overall responsibility for the credit risk function. The GCCO chairs the Credit Risk Committee and, with the CRO, co-chairs the Group's Provisions Committee.
Governance	Credit Risk committee	Authority over risk appetite (within the appetite set by the board), strategy, frameworks and policy as well as oversight of the Group's credit profile.
	Provisions Committee (1,2)	Authority over provisions adequacy and approval of recommendations from business provisions committees in accordance with approval thresholds.
Risk appetite	Concentration frameworks - Wholesale ° Single name ° Sector ° Country ° Product and asset class - Personal credit appetite framework Reputational and environmental, social and ethical frameworks Credit policy	Frameworks are maintained to ensure that the risk of an outsized loss due to a concentration to a particular borrower, sector, product type or country remains within appetite. The credit frameworks are aligned to the Group's risk appetite framework. The Group uses a product and asset class framework to control credit risk for its Personal businesses. The framework sets limits that measure and control the quality of both existing and new business for each relevant franchise or segment.
Controls and risk assurance	Control assurance Quality assurance Model risk management	Credit policy standards are in place for both Wholesale and Personal portfolios and are expressed as a set of mandatory controls. Assurance activities, as defined by credit policy, are undertaken by an independent assurance function.
Credit stewardship	Credit assessment standards Credit risk mitigation and collateral Credit documentation Regular portfolio/customer review Problem debt identification and management	Credit risk stewardship takes place throughout the customer lifecycle, from initial credit approval and on a continuous basis thereafter. The methodology applied for assessing and monitoring credit risk varies between customer types and segments.
Customers	Segmentation	Customers are managed differently, reflecting different customer types and risks. Wholesale customers are grouped by industry clusters and managed on an individual basis (includes Corporates, Banks and Financial Institutions). Personal customers are grouped into portfolios of similar risk and managed on a portfolio basis (3).

Notes:
(1) Co-chair with RBS Group Chief Risk Officer.
(2) Authority is delegated by Executive Risk Forum.
(3) For further information on the Group's provisioning and impairment practices refer to page 106.

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Risk appetite*

Risk appetite across all risk types is set using specific quantitative targets under stress, including earnings volatility and capital adequacy. The credit risk appetite frameworks have been designed to reflect factors that influence the ability to meet those targets. Tools such as stress testing and economic capital are used to measure credit risk volatility and develop links between the credit risk appetite frameworks and risk appetite targets. The frameworks are supported by a suite of policies and transaction acceptance standards that set out the risk parameters within which franchises must operate. For further information of the specific frameworks for Wholesale and Personal refer to pages 74 and 88 respectively.

Risk measurements and models*

Credit risk assets

The Group uses a range of measures for credit risk exposures. The internal measure used, unless otherwise stated, is credit risk assets (CRA) consisting of:

- Lending exposure - measured using drawn balances (gross of impairments). Comprises cash balances at central banks as well as loans and advances to banks and customers.
- Counterparty exposures - measured using the mark-to-market value of derivatives after the effect of enforceable netting agreements and regulator-approved models but before the effect of collateral. Calculations are gross of credit value adjustments.
- Contingent obligations - measured using the value of the committed amount and including primarily letters of credit and guarantees.

CRA exclude issuer risk (primarily debt securities) and securities financing transactions. CRA take account of regulatory netting although, in practice, obligations are settled under legal netting arrangements that provide a right of legal set-off but do not meet the offset criteria under IFRS.

Risk models

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

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

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Credit risk: management basis continued

Changes to credit models

The Group reviews and updates models on an ongoing basis in order to reflect the impact of more recent data, changes to products and portfolios, and new regulatory requirements. Extensive changes were made to wholesale models between 2012 and 2014. To a lesser extent, the impact of these changes continued through 2015, resulting in some downwards rating migrations across internal asset quality bands. For further information, refer to the Asset quality section on page 102.

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

For more information on model governance and review refer to the Model section on page 33.

Risk mitigation*

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

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

The business and credit teams are supported by specialist in-house documentation teams. The Group uses industry-standard loan and security documentation wherever possible. However, when non-standard documentation is used, external lawyers are employed to review it on a case-by-case basis. Mitigants (including any associated insurance) are monitored throughout the life of the transaction to ensure that they perform as anticipated. Similarly, documentation is also monitored to ensure it remains enforceable.

For further information refer to the sub-sections on Wholesale credit risk management and Personal credit risk management.

Counterparty credit risk

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

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

Collateral may consist of either cash or securities. In the case of derivatives, collateral generally takes the form of cash. In the case of securities financing transactions, collateral usually takes the form of debt securities and, to a much lesser extent, equity securities at the outset. However, if the value of collateral falls relative to the obligation, the Group may require additional collateral in the form of cash (variation margin). The vast majority of agreements are subject to daily collateral calls with collateral valued using the Group's internal valuation methodologies.

Industry standard documentation - such as master repurchase agreements and credit support annexes accompanied by legal opinion - is used for financial collateral taken as part of trading activities.

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

Risk assessment and monitoring

Practices for credit stewardship - including credit assessment, approval and monitoring as well as the identification and management of problem debts - differ between the wholesale and personal portfolios. For further information refer to the relevant sub-sections on pages 74 and 88. A key aspect of credit risk stewardship is ensuring that, when signs of impairment are identified, appropriate impairment provisions are recognised.

Impairment, provisioning and write-offs

In the overall assessment of credit risk, impairment, provisioning and write-offs are used as key indicators of credit quality. The impairment, provisioning and write-off processes are described in more detail below.

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Impairment

A financial asset is impaired if there is objective evidence that the amount, or timing, of future cash flows has been adversely affected since its initial recognition. Refer to accounting policies on page 154 for details regarding the quantification of impairment losses.

Days-past-due measures are typically used to identify evidence of impairment. In both Wholesale and Personal portfolios, a period of 90 days past due is used. In sovereign portfolios, the period used is 180 days past due. Indicators of impairment include the borrower's financial condition; a forbearance event; a loan restructuring; the probability of bankruptcy; or any evidence of diminished cash flows.

Provisioning

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

Provision method	Customer type	Quantification method	Key factors considered
Individual	Impaired, individually significant	Case-by-case assessment of future cash flows	• Customer and guarantor performance. • Future value of collateral. • Future economic conditions based on factors available at the time.
Collective	Impaired but not individually significant, grouped into homogenous portfolios	Quantitative review of relevant portfolio	• Level of arrears. • Value of security. • Historical and projected cash recovery trends. • Current economic conditions. • Operational processes. • Latest cash collection profile.
Latent	Not impaired	PD% x LGD% x EAD x Emergence Period	• For wholesale customers PD, LGD and EAD values are used. • For personal, calculations are performed at portfolio level by product (e.g. mortgages, credit cards or unsecured loans). • Portfolio-level emergence periods are based on products or businesses with similar homogenous characteristics. Emergence periods range from 120 to 274 days.

Credit risk: management basis continued

Refer to pages 106 to 111 for an analysis of impaired loans, related provisions and impairments. Refer to page 154 for details of accounting policies. For details on collateral, refer to the Counterparty credit risk section on page 70 as well as the Wholesale and Personal risk mitigation sections on pages 74 and 88.

The Restructuring credit team will ultimately recommend or approve any provision that may be required.

Sensitivity of impairments to assumptions

Key assumptions relating to impairment levels relate to economic conditions, the interest rate environment, the ease and timing of enforcing loan agreements in varying legal jurisdictions and the level of customer co-operation.

In addition, for secured lending, key assumptions relate to the valuation of the security and collateral held, as well as the timing and cost of asset disposals based on underlying market depth and liquidity. Assessments are made by relationship managers on a case-by-case basis for individually-assessed provisions and are validated by credit teams. For individual impairments greater than £1 million, oversight is provided by the RBS Group Provisions Committee.

Available-for-sale portfolios

Available-for-sale portfolios are also regularly reviewed for evidence of impairment, including: default or delinquency in interest or principal payments; significant financial difficulty of the issuer or obligor; and increased likelihood that the issuer will enter bankruptcy or other financial reorganisation.

Determining whether evidence of impairment exists requires the exercise of management judgement. It should be noted that the following factors are not, of themselves, evidence of impairment, but may be evidence of impairment when considered with other factors:

- Disappearance of an active market because an entity's financial instruments are no longer publicly traded.
- A downgrade of an entity's credit rating.
- A decline in the fair value of a financial asset below its cost or amortised cost.

Write-offs

Impaired loans and receivables are written-off when there is no longer any realistic prospect of recovery of part, or the entire loan. For loans that are individually assessed for impairment, the timing of write-off is determined on a case-by-case basis. Such loans are reviewed regularly and write-offs may be prompted by bankruptcy, insolvency, forbearance and similar events. For details of the typical time frames, from initial impairment to write off, for collectively assessed portfolios refer to the accounting policies section on 155.

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

Portfolio overview*

2015	Wholesale							Total excluding Citizens	Citizens	Total
	Personal (1) £m	Banks and Other FIs £m	Sovereigns £m	Property £m	Natural Resources £m	Retail & Leisure £m	Other £m	£m	£m	£m
UK	137,294	27,410	45,604	38,900	7,224	14,702	39,595	310,729	n/a	310,729
RoI (2)	14,347	876	1,610	1,755	417	1,212	2,323	22,540	n/a	22,540
Other Western Europe	565	24,856	20,237	2,756	2,351	924	6,559	58,248	n/a	58,248
North America	302	8,634	11,292	601	911	776	2,047	24,563	n/a	24,563
RoW (3)	2,835	6,274	3,437	830	1,253	204	7,793	22,626	n/a	22,626
Total	155,343	68,050	82,180	44,842	12,156	17,818	58,317	438,706	n/a	438,706
Watch Red	—	20	106	554	415	286	811	2,192	n/a	2,192
AQ10	6,302	274	1	4,508	283	803	1,932	14,103	n/a	14,103
2014										
UK	129,091	26,388	45,068	44,393	7,825	15,489	40,093	308,347	60	308,407
RoI (2)	16,064	1,399	647	7,571	465	1,913	3,096	31,155	22	31,177
Other Western Europe	738	31,297	5,516	4,274	3,509	1,305	9,916	56,555	99	56,654
North America	281	11,353	25,035	921	4,750	1,043	6,670	50,053	63,850	113,903
RoW (3)	2,406	11,967	2,250	1,802	5,356	1,090	15,611	40,482	167	40,649
Total	148,580	82,404	78,516	58,961	21,905	20,840	75,386	486,592	64,198	550,790
Watch Red	—	95	127	1,122	563	351	1,022	3,280	554	3,834
AQ10	7,871	524	1	14,676	219	2,313	3,588	29,192	660	29,852

Notes:
(1) Personal includes business customers in Business Banking
(2) RoI: Republic of Ireland.
(3) Rest of World comprises Asia Pacific, Central and Eastern Europe, the Middle East, Central Asia and Africa, and supranationals such as the World Bank.

Key points

The following key portfolios are either designated high-oversight sectors under the sector framework or constitute a material proportion of CRAs and are discussed in more detail below.

Commercial Real Estate (CRE) (in Property) - refer to page 80;
Oil & Gas (in Natural Resources) - refer to page 83;
Mining & Metals (in Natural Resources) - refer to page 85;
Automotive - refer to page 86;
Shipping (in Other) - refer to page 87; and
Personal, including mortgages - refer to page 90.

- The increase in the Personal portfolio was predominantly driven by activity in the UK and is in line with RBS strategy to expand this portfolio. For further information on Personal refer to page 88.
- The decrease in the Wholesale portfolio was observed in a majority of sectors reflecting a continued focus on risk reduction and improving overall credit quality. The increase in sovereigns reflected Treasury activity.
- The number of Watch Red customers continued to decrease during 2015 due to a reduced flow of new cases as well as through customers being taken off Watch as their financial position improved.
- The reduction in AQ10 assets during the year was primarily due to RCR, within Capital Resolution, completing its targeted run-down by the end of 2015.

*unaudited

Credit risk: management basis continued

Wholesale credit risk management

This section sets out further detail on the Group's approach to credit risk management for its Wholesale customers. Four formal frameworks are used to manage Wholesale credit concentration risks within the Group's risk appetite. These frameworks are regularly reassessed to ensure they remain appropriate for the Group's varied business franchises, economic and market conditions and to reflect refinements in risk measurement models as well as agreed risk appetite.

A summary of the frameworks is set out below.*

Concentration framework	Single name (SNC)	Sector	Product and asset class	Country
Risk addressed	Outsized loss due to concentration on a single borrower or borrower group.	Concentration in a single sector or across sectors that are susceptible to similar stress events.	Concentration on certain products or asset classes.	Concentration on a particular country.
Basis for classification	Size or LGD - based on net customer exposure for a given probability of default.	Size - based on exposure; and Risk - based on Economic Capital and other qualitative factors.	Size - based on exposure to a product or asset class.	Size - based on exposure to a particular country.
Limit types	Customer exposure and LGD limits relative to PD.	Bank-wide and franchise sector and sub-sector exposure limits.	Bank-wide and franchise product/asset class exposure limits and sub-limits.	Bank-wide country limits.
Controls within the framework	Elevated approval requirements, monitoring and reporting, the requirement for regular reviews and for plans to address any exposures in excess of limit.			
Exposure measure (net/gross)	Both net and gross of "eligible" mitigants. To be eligible under the framework, mitigants must be legally enforceable, structurally effective and of appropriate maturity.	Gross exposure to a sector/sub-sector.	Net/gross - dependent on type of product.	Net of provisions and risk transfer.
Recent developments	The aggregate SNC exposures remain outside the Group's long-term risk appetite. However material reductions were achieved during the year. There was a 40% decrease in the number of SNC excesses during 2015 (15% increase in exposure - however a risk mitigation strategy is in place to reduce this). The top ten SNC excesses comprised 90% of total SNC excesses.	Risk appetite for the Oil & Gas, Retail & Leisure, Automotive and Commercial Real Estate sectors was reduced. This took into account market/economic conditions and the successful execution of the RCR strategy to reduce exposures to these sectors.	Risk appetite limits were reduced taking account of the revised risk appetite associated with the restructured CIB business.	Risk appetite limits were reduced for exit countries taking account of the revised risk appetite and international strategy.

*unaudited

Risk assessment*

Before credit facilities are made available to customers a credit assessment is undertaken. The assessment process is the same for all customers. However, in the Group, credit risk management is organised in terms of the complexity of the assessment rather than aligned to franchises. Capital Resolution is not managed separately but is shown in tables to aid understanding of the size of the exit portfolio. Credit is only granted to customers following joint approval by an approver from the business and the credit risk function.

These approvers act within a delegated approval authority under the wholesale Credit Authorities Framework (CAF) approved by the Executive Risk Forum.

The level of delegated authority held by approvers is dependent on their experience and expertise. Only a small number of senior executives hold the highest authority provided under the CAF. Both business and credit approvers are accountable for the quality of each decision taken but the credit risk approver holds ultimate sanctioning authority.

In 2015, new Transaction Acceptance Standards (TAS) were introduced to provide more detailed transactional lending and risk acceptance guidelines which are one of the tools to control risk appetite at the customer/transaction level. TAS are supplementary to Credit Policy.

When assessing credit risk the following must be considered at a minimum:

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

Where the customer is part of a group, the credit assessment considers aggregated credit risk limits for the customer group as well as the nature of the relationship with the broader group (e.g. parental support) and its impact on credit risk.

At a minimum, credit relationships are reviewed and re-approved annually. The renewal process addresses borrower performance, including reconfirmation or adjustment of risk parameter estimates; the adequacy of security; compliance with terms and conditions; and refinancing risk.

Risk mitigation

The Group mitigates credit risk through the use of netting, collateral and market standard documentation, depending on the nature of the counterparty and its assets. The most common types of mitigation are:

- Commercial real estate - Refer to CRE section on page 80.
- Other physical assets - Including stock, plant, equipment, machinery, vehicles, ships and aircraft. Such assets are suitable collateral only if the Group can identify, locate, and segregate them from other assets on which it does not have a claim. The Group values physical assets in a variety of ways, depending on the type of asset and may rely on balance sheet valuations in certain cases.
- Receivables - These are amounts owed to the Group's counterparties by their own customers. The Group values them after taking into account the quality of its counterparty's receivable management processes and excluding any that are past due.
- Financial collateral - Refer to Counterparty credit risk section on page 70.

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

*unaudited

Credit risk: management basis continued

Shipping valuations - Vessel valuations are performed by Group-approved brokers. Each broker has a number of vessels to value according to its specific area of expertise. Valuations are undertaken on a desktop basis on a willing buyer/willing seller and charter-free basis. All valuations are in writing, instructed by and addressed to the Group. Valuations are performed on a quarterly basis. From time to time, particularly for facilities showing increased signs of financial stress, a more formal valuation will be obtained.

Commercial real estate valuations - The Group has a panel of chartered surveying firms that cover the spectrum of geography and property sectors in which the Group takes collateral. The Group has a programme that identifies suitable valuers for particular assets. They are contracted through a single service agreement to ensure consistency of quality and advice. Valuations are commissioned when an asset is taken as security; a material increase in a facility is requested; or an event of default is anticipated or has occurred. In the UK, the Group also applies an independent third-party market indexation to update external valuations once they are more than a year old.

Problem debt management

*Early problem identification**

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

The RBS Group has reviewed the Watchlist process and will implement a new Risk of Credit Loss framework in early 2016. This will ensure the problem debt portfolio is managed consistently and efficiently, with added focus on customers whose credit profiles have deteriorated outside original risk appetite.

*Watchlist**

For customers not managed in Capital Resolution, there are three Watch classifications - Amber, Red and Black - reflecting progressively deteriorating conditions.

Watch Amber customers are performing customers who show early signs of potential financial difficulty, or have other characteristics that warrant closer monitoring.

Watch Red customers are performing customers who show signs of declining creditworthiness and so require active management. When a customer is classified as Watch Red, the Restructuring team engaged to consider whether the relationship should be transferred to them. Watch Red customers who continue to be managed outside of restructuring tend to be those requiring specialist subject matter expertise that is only available outside of Restructuring.

The Watch Black portfolio includes AQ10 exposures.

*unaudited

Once on the Watchlist a number of mandatory actions are taken, including a review of the customer's credit grade and facility and security documentation. Depending on the severity of the financial difficulty and the size of the exposure, the customer relationship strategy is reassessed by credit officers, by specialist credit risk or relationship management units in the relevant business or by Restructuring.

In more material cases, a forum of experienced credit, portfolio management and remedial management specialists in either the relevant business or Restructuring may reassess the customer relationship strategy.

Appropriate corrective action is taken when circumstances emerge that may affect the customer's ability to service its debt. Such circumstances include deteriorating trading performance, imminent breach of covenant, challenging macroeconomic conditions, a late payment or the expectation of a missed payment.

Remediation strategies available in the business include granting a customer various types of concessions. Any decision to approve a concession will be a function of specific country and sector appetite, the credit quality of the customer, the market environment and the loan structure and security. For further information, refer to the Wholesale forbearance section below.

Other potential outcomes of the relationship review are to: take the customer off the Watchlist; offer additional lending and continue monitoring; transfer the relationship to Restructuring if appropriate; or exit the relationship altogether.

Customers managed in Capital Resolution are by their nature subject to heightened scrutiny and regular review against specific disposal plans. Capital Resolution customers are separately identified in the Group's internal Watchlist reporting, with their Watchlist classification based on asset quality.

Restructuring*

The Restructuring team manages customer relationships with the RBS Group's Wholesale problem debt portfolio. The factor common to all customers with Restructuring involvement is that the RBS Group's exposure is outside risk appetite. The primary function of Restructuring is to restore customers to an acceptable credit profile, minimise losses to the RBS Group and protect the RBS Group's capital.

Specialists in Restructuring work with customers experiencing financial difficulties, and showing signs of financial stress, with the aim of restoring their business to financial health whenever possible. The objective is to find a mutually acceptable solution, including restructuring of existing facilities, repayment or refinancing if that is the customer's preferred option.

Specialists within Restructuring conduct a detailed assessment of the viability of the business, as well as the ability of management to deal with the causes of financial difficulty, focusing on both financial and operational issues. Following the assessment, options which may include forbearance and/or restructuring of facilities are developed. Credit risk decisions, including reviewing and approving any operational and financial restructuring solutions in relation to these customers, are made by a dedicated Restructuring Credit team, which is part of the credit risk management function.

Where a solvent solution is not possible, insolvency may be considered as a last resort. However, helping the customer return to financial health and restoring a normal banking relationship is always the desired goal.

Forbearance

Forbearance takes place when a concession is made on the contractual terms of a loan in response to a customer's financial difficulties. Concessions granted where there is no evidence of financial difficulty, or where any changes to terms and conditions are within usual risk appetite (for a new customer), or reflect improving credit market conditions for the customer, are not considered forbearance.

The aim of forbearance is to restore the customer to financial health while minimising risk to the Group. To ensure that forbearance is appropriate for the needs and financial profile of the customer, minimum standards are applied when assessing, recording, monitoring and reporting forbearance.

Types of wholesale forbearance

The type of forbearance offered is tailored to the customer's individual circumstances. For wholesale customers forbearance may involve the following types of concessions:

- Covenant waiver
  A recalibration of covenants or a covenant amendment may be used to cure a potential or actual covenant breach. In return for this relief, the Group would seek to obtain a return commensurate with the risk that it is required to take. The increased return for the increased risk can be structured flexibly to take into account the customer's circumstances. For example it may be structured as either increased margin on a cash or payment-in-kind basis, deferred-return instruments or both. While the Group considers these types of concessions qualitatively different from other forms of forbearance, they constitute a significant proportion of Wholesale forborne loans and are therefore included in these disclosures.
- Amendment to margin
  Contractual margin may be amended to bolster the customer's day-to-day liquidity to help sustain its business as a going concern. This would normally be a short-term solution. the Group would seek a return commensurate to the risk that it is required to take.
- Payment concessions and loan rescheduling (including extensions in contractual maturity)
  May be granted to improve the customer's liquidity or on the expectation that the customer's liquidity will recover when market conditions improve. In addition, they may be granted if the customer will benefit from access to alternative sources of liquidity, such as an issue of equity capital. These options have been used in CRE transactions, particularly during periods where a shortage of market liquidity has ruled out immediate refinancing and made short-term collateral sales unattractive.
- Debt forgiveness/debt for equity swap
  May be granted where the customer's business condition or economic environment is such that it cannot meet obligations and where other forms of forbearance are unlikely to succeed. Debt forgiveness can be used for stressed corporate transactions and is typically structured on the basis of projected cash flows from operational activities, rather than underlying tangible asset values. Provided that the underlying business model, strategy and debt level are viable, maintaining the business as a going concern is the preferred option, rather than realising the value of the underlying assets.

Loans may be forborne more than once, generally where a temporary concession has been granted and circumstances warrant another temporary or permanent revision of the loan's terms. All customers are assigned a PD and related facilities an LGD. These are re-assessed prior to finalising any forbearance arrangement in light of the loan's amended terms and any revised grading is incorporated in the calculation of the impairment loss provisions for the Group's wholesale exposures.

The ultimate outcome of a forbearance strategy is unknown at the time of execution. It is highly dependent on the cooperation of the borrower and the continued existence of a viable business. Where forbearance is no longer viable, the Group will consider other options such as the enforcement of security, insolvency proceedings or both. The following are generally considered to be options of last resort:

- Enforcement of security or otherwise taking control of assets - Where the Group holds collateral or other security interest and is entitled to enforce its rights, it may enforce its security or otherwise take control of the assets. The preferred strategy is to consider other possible options prior to exercising these rights.
- Insolvency - Where there is no suitable forbearance option or the business is no longer sustainable, insolvency will be considered. Insolvency may be the only option that ensures that the assets of the business are properly and efficiently distributed to relevant creditors.

*unaudited

Credit risk: management basis continued

Provisions for forborne wholesale loans are assessed in accordance with normal provisioning policies (refer to Impairment loss provision methodology). The customer's financial position and prospects as well as the likely effect of the forbearance, including any concessions granted, are considered in order to establish whether an impairment provision is required.

Wholesale loans granted forbearance are individually assessed in most cases and are not therefore segregated into a separate risk pool.

Forbearance may result in the value of the outstanding debt exceeding the present value of the estimated future cash flows. This may result in the recognition of an impairment loss or a write-off.

For performing loans, credit metrics are an integral part of the latent provision methodology and therefore the impact of covenant concessions will be reflected in the latent provision. For non-performing loans, covenant concessions will be considered in determining the overall provision for these loans.

In the case of non-performing forborne loans, the loan impairment provision assessment almost invariably takes place prior to forbearance being granted. The amount of the loan impairment provision may change once the terms of the forbearance are known, resulting in an additional provision charge or a release of the provision in the period the forbearance is granted.

The transfer of wholesale loans subject to forbearance from impaired to performing status follows assessment by relationship managers and the Restructuring credit risk function. When no further losses are anticipated and the customer is expected to meet the loan's revised terms, any provision is written off and the balance of the loan returned to performing status. This course of action is not dependent on a specified time period and follows the credit risk manager's assessment that it is appropriate.

Flow into forbearance

The table below shows the value of loans (excluding loans where the Group has initiated recovery procedures) where forbearance was completed during the year, by sector and types. This only includes the forborne facility exposure. No exit criteria are currently applied.

	2015				2014			
Wholesale forbearance during the year by sector	Performing £m	Non-performing £m	Total £m	Provision coverage (1) %	Performing £m	Non-performing £m	Total £m	Provision coverage (1) %
Property	482	993	1,475	45	1,051	4,362	5,413	66
Natural resources of which:								
- Oil & Gas	478	23	501	11	258	—	258	64
- Mining & Metals	28	1	29	46	27	1	28	64
- Electricity	44	27	71	57	21	17	38	47
- Water & Waste	45	1	46	25	51	—	51	100
Transport	147	81	228	29	261	233	494	32
Retail & Leisure	275	147	422	32	430	552	982	51
Services	512	193	705	44	562	351	913	53
Other	247	134	381	47	299	231	530	56
Total	2,258	1,600	3,858	43	2,960	5,747	8,707	62

Note:
(1) Provision coverage reflects impairment provision as a percentage of non-performing loans.

Forbearance arrangements

The table below shows the incidence of the main types of Wholesale renegotiations.

Wholesale renegotiations during the year by type (1,2)	2015 £m	2014 £m
Payment concessions	2,542	7,014
Non-payment concessions	1,316	1,692
Total	3,858	8,706

Notes:
(1) Forbearance arrangements in 2014 included £133 million of payment and £177 million of non-payment refinancing concessions respectively; refinancing forbearance arrangements in 2015 totalled nil.
(2) Previously reported forbearance types are classified as non-payment (covenant concessions, release of security) and payment (payment concessions and loan rescheduling, forgiveness of all or part of the outstanding debt, variation in margin, standstill agreements).

Key points

- For Wholesale, the decreased flow into forbearance during 2015, in comparison to 2014, reflected improving market conditions and a reduction in exit portfolios through RCR's disposal strategy. 41% of the total forbearance granted was related to non-performing loans with a provision coverage of 43% (2014 - 62%).
- The decrease in completed forbearance during 2015 compared with 2014 was in line both with improving market conditions, the RCR disposal strategy and portfolio reduction strategies. Year-on-year analysis of forborne loans may be skewed by individual material cases during a given year.
- Loans totalling £1.7 billion were granted approval for forbearance but had not yet reached legal completion at 31 December 2015 (2014 - £4.3 billion). These exposures are referred to as "in process" and are not included in the tables above. 64% (£1.1 billion) of these "in process" exposures related to non-performing customers, with associated provision coverage of 30%. 36% (£0.6 billion) related to performing loans. The principal types of arrangements offered were payment concessions and loan rescheduling.
- Forbearance in the Natural Resources sector cluster showed a material increase over 2015, given the sector's challenges. (Refer to page 82 for further information).
- Forbearance in the Transport sector cluster was historically driven by RCR exposure to the Shipping sector. There have been lower levels of forbearance in the Shipping portfolio in 2015 as a result of the RCR disposal strategy. There was an increase in the volume of Non-RCR Shipping exposures granted forbearance, though these were on average smaller than those granted forbearance in 2014. (Refer to page 87 for further information).
- The value of loans forborne during 2014 and 2015 and still outstanding at 31 December 2015 was £5.6 billion (2014 - £12.2 billion), of which £1.7 billion related to arrangements completed during 2014 (2014 - £3.4 billion completed in 2013).
- Additional provisions charged in 2015 and relating to loans forborne during 2014 totalled £0.2 billion, predominantly driven by RCR and Restructuring cases. Provision coverage of these loans at 31 December 2015 was 66%.
- £0.9 billion of completed forbearance granted during the year related to exposures managed by RCR. RCR uses forbearance as a tool to assist with the orderly realisation of assets.
- Non-RCR customers were granted forbearance on loan facilities totalling £3.0 billion, of which £1.3 billion was managed by Restructuring during 2015. This equated to 48% of loans managed by Restructuring (excluding loans to customers where recovery procedures have commenced).
- By value, 90% (£1.5 billion) of the performing non-RCR loans granted forbearance in 2014 remained performing at 31 December 2015.
- Provisions for the non-performing loans disclosed above are individually assessed and therefore not directly comparable across periods. Provision coverage decreased in 2015, which is reflective of the lower proportion of the forborne portfolio that RCR customers represent compared to the prior year. RCR customers have a higher provision coverage than the non-RCR portfolio given the nature of the RCR strategy.
- The data presented in the tables above include loans forborne during 2015 and 2014. Until April 2014 a reporting threshold was in place which ranged from nil to £3 million after which no thresholds were in use. A number of immaterial portfolios have forbearance assessed under a portfolio approach.

Credit risk: management basis continued

Key credit portfolios

Commercial real estate

The CRE sector relates to lending activity for the development of, and investment in, commercial and residential properties.

A dedicated portfolio controls team is responsible for portfolio strategy, credit risk appetite and policies, as well as oversight of valuations and environmental frameworks. The sector is reviewed regularly at senior executive committees. Reviews include portfolio credit quality, capital consumption and control frameworks.

In Commercial Banking, lending applications are reviewed by specialist CRE transactional credit teams, including a dedicated development team. Lending guidelines and policy are informed by lessons learned from the 2008 financial crisis.

New business is monitored and controlled against agreed underwriting standards. Sub-sector and asset class limits are used to restrict exposure to emerging risks when appropriate. This activity is reviewed and monitored on a regular basis.

CRE occupier market fundamentals have improved gradually over the last year as a result of stable economic growth. Areas of weakness remain in secondary, regional retail and provincial office locations but, overall, vacancy rates are declining and rental values are showing signs of growth across a wide range of geographies and sub-sectors. The strongest rental growth to date has been in and around London, but it is now spreading to the wider south-east of England area and key regional centres. Over 2015, CRE investment activity was marginally down on the record levels seen in 2014, despite a very strong start in the first half of the year. There was continued demand from overseas investors who accounted for 50% of the total value of all UK commercial property acquisitions in 2015.

CRE exposure by geography and investment and development*

	Investment			Development			Overall
By geography	Commercial £m	Residential £m	Total £m	Commercial £m	Residential £m	Total £m	total £m
2015							
UK	16,620	4,305	20,925	717	3,597	4,314	25,239
RoI	627	156	783	200	408	608	1,391
Other Western Europe	614	17	631	17	6	23	654
US	263	1	264	—	—	—	264
RoW	59	3	62	8	12	20	82
	18,183	4,482	22,665	942	4,023	4,965	27,630
Of which: Capital Resolution	1,935	102	2,037	268	504	772	2,809
Williams & Glyn	2,100	648	2,748	83	488	571	3,319
2014							
UK	18,038	4,901	22,939	989	4,944	5,933	28,872
RoI	2,150	595	2,745	1,109	2,969	4,078	6,823
Other Western Europe	1,218	50	1,268	190	20	210	1,478
US	404	—	404	—	59	59	463
RoW	414	26	440	34	191	225	665
Total excluding Citizens	22,224	5,572	27,796	2,322	8,183	10,505	38,301
Citizens	3,658	1,358	5,016	—	—	—	5,016
Total	25,882	6,930	32,812	2,322	8,183	10,505	43,317
Of which: Williams & Glyn	2,194	735	2,929	29	386	415	3,344

Note:
(1) Geography splits are based on country of collateral risk.

Key points

- Overall gross CRE lending fell due to asset sales, repayments and write-offs.
- Further divestments of Williams & Glyn (£3.3 billion) and Capital Resolution (£2.8 billion) will leave the CRE portfolio concentrated in the UK and Ireland.
- Commercial Banking manages the majority (£18.1 billion) of the remaining CRE portfolio. The Commercial Banking portfolio shape and size remained broadly stable during 2015, with significant exposure (£12.2 billion) in the commercial investment sub-sector.

*unaudited

CRE exposure by LTV band*

The table below provides a breakdown of the CRE portfolio by LTV band, along with provision coverage.

	2015			2014		
Loan-to-value ratio	Performing £m	Non-performing £m	Total £m	Performing £m	Non-performing £m	Total £m
<= 50%	11,549	126	11,675	9,497	263	9,760
> 50% and <= 70%	6,973	190	7,163	7,299	469	7,768
> 70% and <= 90%	1,237	647	1,884	1,748	947	2,695
> 90% and <= 100%	210	291	501	335	250	585
> 100% and <= 110%	187	121	308	182	360	542
> 110% and <= 130%	261	222	483	362	639	1,001
> 130% and <= 150%	62	127	189	120	532	652
> 150%	386	707	1,093	367	4,655	5,022
Total with LTVs	20,865	2,431	23,296	19,910	8,115	28,025
Minimal security (1)	6	156	162	33	3,206	3,239
Other	2,847	1,325	4,172	4,569	2,468	7,037
Total	23,718	3,912	27,630	24,512	13,789	38,301
Total portfolio average LTV (2)	54%	177%	66%	56%	291%	123%

Notes:
(1) Total portfolio average LTV is quoted net of loans with minimal security given that the anticipated recovery rate is less than 10%. Provisions are marked against these loans where required to reflect the relevant asset quality and recovery profile.
(2) Weighted average by exposure.

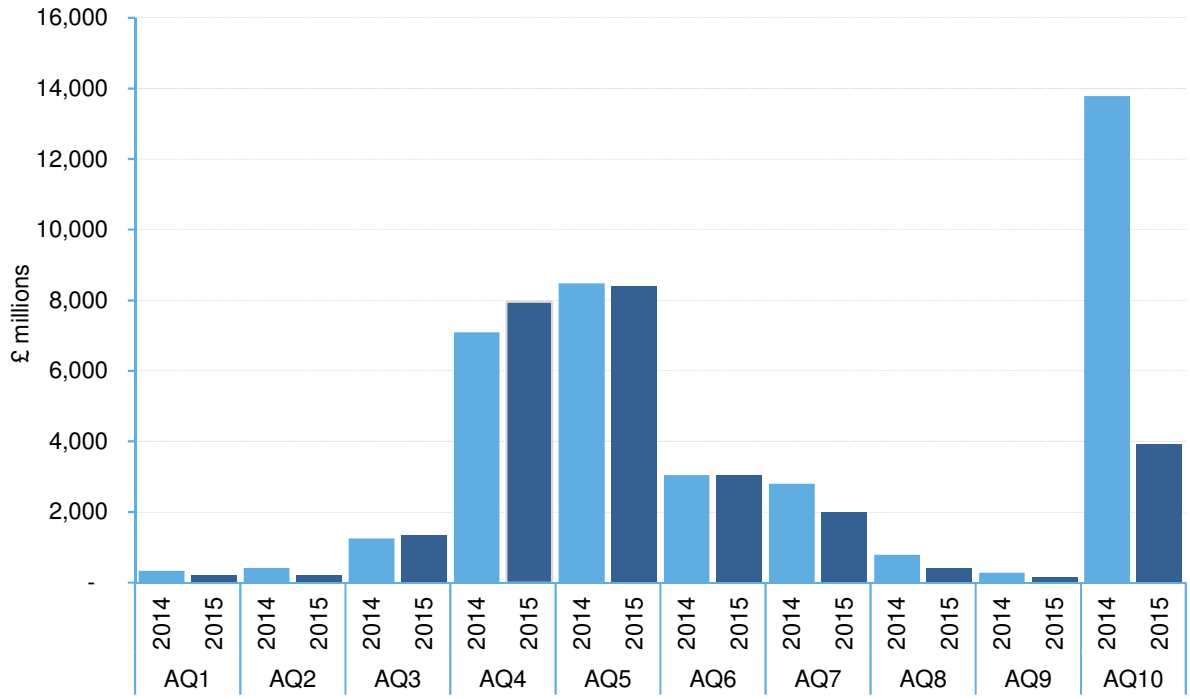
Key points

- The LTVs in the table above continued to be affected by the legacy portfolio. Loans originated during 2015 are considered in line with current market terms in relation to LTV and ICR.
- The proportion of the book with LTV higher than 75% reduced year on year, due to maintained underwriting standards applied on new lending and improved economic conditions in the markets in which the Group operates.
- Exposures with LTVs greater than 100% are predominantly legacy deals.
- Accelerated divestment of legacy exits assets has reduced the amount of non-performing exposure with minimal security.
- The remaining non-performing exposure with minimal security has a 94% provision coverage in place. Total individual provisions for the non-performing CRE book are £1.5 billion and collective provisions of £0.4 billion, which equates to a provision coverage of 50%.
- The exposure in Other relates predominantly to lending to large corporate entities. It is not asset-backed but secured against corporate balance sheets.
- The weighted average maturity profile for Commercial Banking was three years and two months, which has remained broadly unchanged since 2014.
- Accelerated divestments in Capital Resolution have contributed significantly to the improvement in portfolio quality during the year. £21.1 billion of the portfolio was AQ6 (B+) or better, reflecting maintained underwriting standards and improved economic conditions in the markets in which the Group operates.

*unaudited

Credit risk: management basis continued

Asset quality*



Natural Resources*

The Group's exposure to Natural Resources in terms of CRA and TCE (total exposure including committed but undrawn facilities), is set out below.

	2015				2014	
	CRA £m	Of which: Capital Resolution £m	Total exposure £m	Of which: Capital Resolution £m	CRA £m	Total exposure £m
Oil & Gas	3,475	1,560	6,550	2,064	9,284	21,866
Mining & Metals	1,113	596	2,084	719	2,535	4,571
Electricity	2,744	1,141	7,350	1,843	4,817	16,101
Water & Waste	4,824	3,002	5,938	3,051	5,269	6,706
Natural Resources	12,156	6,299	21,922	7,677	21,905	49,244

Key points

- Oil & Gas: CRA and TCE decreased significantly during 2015. This reflected proactive credit management, continued loan sales and run-off across the CIB portfolio in Asia-Pacific and the US.
- Mining & Metals: the reduction in CRA and TCE during 2015 reflected proactive credit management of more vulnerable sub-sectors. The majority of the exposure is to large international customers and matures within five years.

*unaudited

Oil & Gas*

The tables below provide a breakdown of Oil & Gas sector exposure (including committed but undrawn exposure) split by sub-sector and geography. The analysis is based on the Group's sector concentration framework.

2015	UK £m	RoI £m	Other Western Europe £m	US £m	RoW (1) £m	Total £m
Producers (incl. integrated oil companies)	992	43	773	329	344	2,481
Oilfield service providers	589	1	782	240	251	1,863
Other wholesale and trading activities	326	77	516	68	377	1,364
Refineries	26	2	1	372	17	418
Pipelines	98	—	303	17	6	424
	2,031	123	2,375	1,026	995	6,550
2014						
Producers (incl. integrated oil companies)	1,139	63	1,137	4,996	1,291	8,626
Oilfield service providers	438	4	693	1,086	1,405	3,626
Other wholesale and trading activities	489	135	798	685	974	3,081
Refineries	50	24	154	2,720	794	3,742
Pipelines	118	—	50	2,420	203	2,791
	2,234	226	2,832	11,907	4,667	21,866

Note:
(1) Rest of World comprises Asia Pacific, Central and Eastern Europe, the Middle East, Central Asia and Africa.

*unaudited

Credit risk: management basis continued

Key points

- Oil prices fell materially during 2015 reaching a 12-year low by 31 December 2015. Market expectations are for oil prices to continue to be weak in the short to medium-term as a result of global oversupply due to OPEC maintaining a high production strategy.
- During 2015, the RBS Group carried out in-depth analysis, stress testing and contagion risk analysis on the Oil & Gas sector. Proactive credit stewardship, together with disposals in the US and Asia-Pacific, reduced the portfolio to £3.5 billion (2014 - £9.3 billion) on a CRA basis, of which £1.6 billion was in Capital Resolution at 31 December 2015. Oil & Gas represented 0.8% of the Wholesale portfolio, excluding Capital Resolution.
- The portfolio management strategy during the year was to focus the portfolio towards investment grade customers with robust credit profiles and strong liquidity to manage through the extended downturn. At 31 December 2015, 65% (2014 - 75%) of the portfolio exposure was investment grade (AQ1-AQ4 or equivalent to BBB- and above). The decrease was mainly due to disposals in the US and Asia-Pacific.
- The sub-sector in which a customer operates is a primary consideration for assessing credit risk. Customers involved in exploration and production (E&P) are most immediately exposed to the oil price decline. Companies involved in this area have already introduced capital spending reductions to conserve cash. In turn, this reduced spending is likely to have an adverse impact on oilfield service providers. This is due to the E&P companies buying fewer products and services from the oilfield service providers, and demanding lower prices for those they do purchase.
- The other principal components of exposure to producers are Integrated Oil Companies (IOCs) and National Oil Companies (NOCs). IOCs and NOCs are less vulnerable to the oil price decline due to scale, diversification and, in the case of NOCs, explicit support from governments.
- Committed lending exposure included legal commitments to syndicated bank facilities with tenors up to five years. These committed facilities are for general corporate purposes - including funding operating needs and capital expenditures - and are available as long as counterparties comply with the terms of the credit agreement. Contingent obligations relate to guarantees, letters of credit and suretyships provided to customers. The Group had no high-yield bond or loan underwriting positions at 31 December 2015 (2014 - US$86 million high-yield loan underwritings in the Americas).
- There was an increase in the number of forbearance events, predominantly involving the relaxation of financial covenants to give customers more financial flexibility. Most forbearance involved customers in the E&P and oilfield services sub-sectors where earnings have been more immediately and materially affected by the downturn.
- The number and value of cases on Watch in the Oil & Gas sector increased during the year. However these related predominantly to Watch Amber classifications as the sector continues to be monitored closely.
- At 31 December 2015, Watch Red exposures outside Capital Resolution totalled £93 million (2014 - £54 million) on a CRA basis.
- The increase in AQ10 reflected changing market conditions which resulted in a limited number of customers experiencing financial stress during the year. AQ10 assets at 31 December 2105 totalled £97 million.

*unaudited

Mining & Metals*

The tables below provide a breakdown of Mining & Metals sector exposure (including committed but undrawn exposure) split by sub-sector and geography. The analysis is based on the RBS Group's sector concentration framework.

2015	UK £m	RoI £m	Other Western Europe £m	US £m	RoW (1) £m	Total £m
Mining	259	—	59	138	382	838
Metals - production	158	4	411	13	47	633
- wholesale	167	3	289	125	29	613
	584	7	759	276	458	2,084
2014						
Mining	183	4	598	237	172	1,194
Metals - production	386	—	86	703	583	1,758
- wholesale	179	6	513	350	571	1,619
	748	10	1,197	1,290	1,326	4,571

Note:
(1) Largely comprises assets covered by the standardised approach, for which a probability of default equivalent to those assigned to assets covered by the internal ratings based approach is not available. Standardised exposures sit predominantly within CPB.

Key points

- Mining & Metals has been reclassified as a high-oversight sector due to rising concerns over the economic slowdown in China.
- Mining & Metals represented 0.4% of the Wholesale portfolio, excluding Capital Resolution.
- The Group's exposure to this sector significantly decreased in 2015 primarily due to proactive credit management and reductions in sub-sectors considered the most vulnerable during the downward phase of this cycle as well as strategic disposals.
- The asset quality of the portfolio remained strong and 63% (2014 - 60%) of the portfolio was investment grade at 31 December 2015. This was the result of management strategy weighted towards market leaders in this sector. The bulk of the exposure was to large international customers.
- The slight increase in AQ10 reflected challenging market conditions. AQ10 assets at 31 December 2015 totalled £48 million.

*unaudited

Credit risk: management basis continued

Transport*

	2015				2014	
	CRA £m	Of which: Capital Resolution £m	Total exposure £m	Of which: Capital Resolution £m	CRA £m	Total exposure £m
Automotive	5,607	221	9,053	228	5,664	9,869
Shipping	7,117	6,540	7,656	6,690	10,065	10,676
Other	7,710	2,515	11,029	3,053	10,834	16,190
Transport	20,434	9,276	27,738	9,971	26,563	36,735

Automotive

Key points

- The global automotive market has shown good levels of growth over the last few years. However, the underlying analysis is somewhat mixed with declines in Latin America and a slow growth trend in China offset by an increase in the US and Western Europe.
- Automotive represented 2.4% of the Wholesale portfolio excluding Capital Resolution.
- The portfolio showed robust credit quality with strong returns and below-average risk with no material changes in risk metrics during the year.
- The Automotive sector was reclassified as high-oversight to allow assessment of contagion risk following the United States Environmental Protection Agency statement on emissions irregularities in the third quarter of 2015. The Group carried out a detailed stress test and an extreme global downturn stress scenario. The results of these tests showed that the credit quality of the portfolio would not be materially affected.
- The portfolio management strategy was focused on supporting counterparties with robust investment grade ratings. The majority of the portfolio comprised UK dealerships and Lombard asset finance facilities together with some international exposures.
- The decrease in AQ10 was predominantly driven by proactive credit management and the run-off of RCR. AQ10 assets at 31 December 2015 totalled £86 million.

*unaudited

Shipping*

Key points

- Shipping exposure was £7.1 billion (2014 - £10.1 billion) at 31 December 2015. £5.9 billion (2014 - £7.9 billion) related to asset-backed ocean-going vessels. As the majority of the Shipping exposure is within Capital Resolution, portfolio metrics quoted below are for Capital Resolution only. The TCE decrease during 2015 reflected scheduled loan repayments, secondary sales and corrections to minimum security covenants and prepayments.
- Sector concentration risks were in the Dry Bulk sub-sector which represented 37% of exposure (2014 - 38%); Tankers at 23% (2014 - 29%) and Containers at 21% (2014 - 17%). The remaining exposures comprised gas (including liquid petroleum and natural gases), 14% (2014 - 10%) and others 5% (2014 - 6%).
- Conditions remained severely depressed in the Dry Bulk sub-sector during 2015, with the Baltic Dry Index falling to a 35-year low as a result of vessel oversupply and a greater-than-expected slowdown in commodity demand from China. Tanker market conditions were favourable and container markets stabilised over the year but remained weak in comparison to historic averages. Most of the Group's portfolio in container ships was insulated by long-term charters, providing more stable long-term fixed cash flows.
- At 31 December 2015, Watch Red exposures (excluding RCR) totalled £60.3 million (2014 - £6.6 million).
- The majority of ship-secured exposure was extended against modern vessels with a low average age of approximately seven years (2014 - 6.4 years). Less than 3% of the total Capital Resolution portfolio is secured by vessels that are more than 15 years old and around 85% (2014 - 87%) was secured by vessels built in the last ten years. Due to strategic considerations, the Group is providing finance on a selective basis against delivered or second-hand vessels and generally at low leverage levels.
- A key protection for the Group was the minimum security covenant. The overall portfolio LTV at 31 December 2015 was 84% (2014 - 77%) reflecting the severe downturn being seen in the Dry Bulk sector. Amortisation across the portfolio was approximately 7% per annum excluding early repayments.
- Asset values fall as markets deteriorate and rise as they improve. Therefore, even if exposure falls, the overall LTV position may rise or fall depending on the underlying value of the vessels. The Dry Bulk sub-sector saw asset value reductions of around 40-50% in 2015 (15-20% in 2014), with 15-20% falls in Q4 2015 alone. This led to a rise in the average LTV. In the Tankers sub-sector, LTVs showed the opposite - a lower leverage due to the stronger market conditions in that sector and amortisation.
- The reduction in AQ10 assets during 2015 was predominantly due to RCR, within Capital Resolution, completing its targeted run-down by the end of 2015. AQ10 assets at 31 December 2015 totalled £362 million with provisions of £135 million.

*unaudited

Credit risk: management basis continued

Personal credit risk management

This section sets out further detail on the Group's approach to credit risk management for its Personal customers.

Risk appetite*

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

Personal credit risk assessment*

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

Personal risk mitigation*

The Group takes collateral in the form of residential property to mitigate the credit risk arising from mortgages and home equity lending. The Group values residential property during the loan underwriting process by either appraising properties individually or valuing them collectively using statistically valid models. The Group updates residential property values quarterly using the relevant residential property index, namely:

Region	*Index used*
UK	Halifax quarterly regional house price index
Northern Ireland	Office for National Statistics house price index
RoI	Central Statistics Office residential property price index

Problem debt management*

Personal customers in financial difficulty are managed through either collections or recoveries functions. Further details of these are set out below:

Collections*

Collections functions in each of the Group's personal businesses provide support to customers who cannot meet their obligations to the Group. Such customers may miss a payment on their loan, borrow more than their agreed limit, or ask for help. Dedicated support teams are also in place to identify and help customers who have not yet missed a payment but may be facing financial difficulty. The collections function uses a range of tools to initiate contact with such customers, establish the cause of their financial difficulty and support them where possible.

*unaudited

In the process, they may consider granting the customer forbearance.

Additionally, in the UK and Ireland support is provided to customers with unsecured loans who establish a repayment plan with the Group through a debt advice agency or a self-help tool. Such "breathing space" suspends collections activity for a 30-day period to allow time for the repayment plan to be put in place. Arrears continue to accrue for customer loans granted breathing space.

If collections strategies are unsuccessful the relationship is transferred to the recoveries team.

Forbearance

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

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

The type of forbearance granted will differ based upon an assessment of the customer's circumstances. Forbearance is granted principally to customers with mortgages and less frequently to customers with unsecured loans.

Forbearance options include, but are not limited to:

- Payment concessions - A temporary reduction in, or elimination of, the periodic (usually monthly) loan repayment is agreed with the customer. At the end of the concessionary period, forborne principal and accrued interest outstanding is scheduled for repayment over an agreed period. Ulster Bank RoI also offers payment concessions in the form of discounted interest rates that involve the forgiveness of some interest.
- Capitalisation of arrears - The customer repays the arrears over the remaining term of the mortgage and returns to an up-to-date position.
- Term extensions - The maturity date of the loan is extended.
- Interest only conversions - The loan converts from principal and interest repayment to interest only repayment on a permanent or, in Ulster Bank RoI only, temporary basis. UK Personal, interest only conversions have not been used to support customers in financial difficulty since 2009.

Types of forbearance offered in the unsecured portfolios vary by reportable segment.

Monitoring of forbearance - The granting of forbearance will only change the delinquency status of the loan in exceptional circumstances, which can include capitalisation of principal and interest in arrears, where the loan may be returned to the performing book if it remains up to date for the duration of the probation period and is deemed likely to continue to do so.

Additionally for some forbearance types a loan may be transferred to the performing book if a customer makes payments that reduce loan arrears below 90 days (Ulster Bank RoI, PBB collections function).

Impairments for forbearance Methodology used for provisioning and impairments for forborne loans will differ depending on whether the loans are performing or non-performing and which business is managing them due to local market conditions. The type of provisioning methodology used and specific factors considered for forborne loans is summarised below:

	Performing forborne loans - Latent calculation(1)	Non-performing forborne loans	
	Difference in PD/LGD used for forborne population	Treatment	Difference in LGD used for forborne population
UK PBB (excl Northern Ireland) and W&G	• Forborne loans form a separate risk pool for 24 months. • Calculation uses the higher of the observed (forborne and total population) default rates, or PD. • An extended emergence period is incorporated for forborne loans.	Collective	• No difference in treatment for non-forborne loans, LGD models unaffected by forbearance.
Northern Ireland	• The PD model used in latent provision calculations is calibrated separately for forborne loans, using information on the historic performance of loans subject to similar arrangements. • An extended emergence period is incorporated for forborne loans.	Collective	• No difference in treatment for non-forborne loans. LGD models unaffected by forbearance.
Ulster Bank RoI	• Forborne loans and previous forborne loans form a separate risk pool taking into account the term of the forbearance treatment and applicable post-probationary periods. • The PD model used in latent provision calculations is calibrated separately for forborne loans, using information on the historic performance of loans subject to similar arrangements. • An extended emergence period is incorporated for forborne loans.	Collective	• Forborne (and previously forborne) loans form a separate risk pool where specific LGDs are allocated using observed performance of these loans.
Private Banking	• An extended emergence period is incorporated for forborne loans.	Individual	• No difference in treatment for non-forborne loans, LGD models unaffected by forbearance.
RBSI	• An extended emergence period may be incorporated for forborne loans via management overlay (reviewed regularly in line with market conditions).	Individual	• No difference in treatment for non-forborne loans, LGD models unaffected by forbearance.

Note:
(1) Once such loans are no longer separately identified, the use of account level PDs, refreshed monthly in the latent provision methodology, captures the underlying credit risk without a material time lag. There is no reassessment of the PD at the time forbearance is granted but the loan is subject to the latent provisioning described above.

Credit risk: management basis continued

Recoveries*

Once a loan has been identified as impaired it is managed by recoveries teams in the relevant businesses. The teams seek to minimise the Group's loss by maximising cash recovery while treating customers fairly.

Where an acceptable repayment arrangement cannot be agreed with the customer litigation may be considered. In the UK and Northern Ireland, no repossession procedures are initiated until at least six months following the emergence of arrears (in the Republic of Ireland, regulations prohibit taking legal action for an extended period). Additionally, certain forbearance options are made available to customers managed by the recoveries function.

Personal portfolio overview: Personal credit risk

	2015					
	UK PBB £m	Ulster Bank RoI £m	Private Banking £m	RBS International £m	W&G £m	Total £m
Mortgages	104,777	13,770	6,565	2,541	10,455	138,108
Of which:						
Interest only variable rate*	13,324	622	3,370	742	1,400	19,458
Interest only fixed rate*	9,117	11	2,089	49	1,077	12,343
Mixed (capital and interest only)*	5,397	86	7	29	748	6,267
Buy-to-let*	14,120	2,005	476	837	1,153	18,591
Forbearance stock: arrears status	3,621	3,515	64	44	521	7,765
Current	3,095	2,143	64	31	438	5,771
1-3 months in arrears	275	653	—	6	46	980
> 3 months in arrears	251	719	—	7	37	1,014
Provisions	180	1,062	4	18	26	1,290
REIL	878	2,550	19	63	123	3,633
Other lending	10,022	280	3,474	63	1,087	14,926
Total lending	114,799	14,050	10,039	2,604	11,542	153,034
Mortgage LTV ratios						
- Total portfolio	56%	83%	54%	57%	54%	59%
- New business	69%	77%	57%	66%	68%	68%
- Performing	56%	80%	54%	57%	54%	58%
- Non-performing	63%	106%	92%	96%	60%	83%

Note:
(1) Impairment provisions include latent provisions.

Mortgage LTV distribution

LTV ratio value 2015	<=50% £m	50% <=70% £m	70% <=90% £m	90% <=100% £m	100% <=110% £m	110% <=130% £m	130% <=150% £m	>150% £m	Total with LTVs £m	Other £m	Total £m
UK PBB	38,932	39,378	22,842	2,749	291	195	103	24	104,514	263	104,777
Performing	*38,447*	*38,662*	*22,372*	*2,650*	*256*	*175*	*91*	*18*	*102,671*	*251*	*102,922*
Non-performing	*485*	*716*	*470*	*99*	*35*	*20*	*12*	*6*	*1,843*	*12*	*1,855*
Ulster Bank RoI	2,549	2,395	2,816	1,279	1,258	2,302	891	280	13,770	—	13,770
Performing	*2,382*	*2,220*	*2,580*	*1,126*	*1,082*	*1,899*	*558*	*92*	*11,939*	—	*11,939*
Non-performing	*167*	*175*	*236*	*153*	*176*	*403*	*333*	*188*	*1,831*	—	*1,831*
Private Banking	2,435	2,847	857	40	17	3	12	21	6,232	333	6,565
Performing	*2,432*	*2,846*	*854*	*31*	*15*	*1*	*12*	*20*	*6,211*	*333*	*6,544*
Non-performing	*3*	*1*	*3*	*9*	*2*	*2*	—	*1*	*21*	—	*21*
RBS International	992	885	536	46	29	25	4	24	2,541	—	2,541
Performing	*987*	*873*	*530*	*41*	*27*	*20*	*3*	*16*	*2,497*	—	*2,497*
Non-performing	*5*	*12*	*6*	*5*	*2*	*5*	*1*	*8*	*44*	—	*44*
W&G	4,185	3,840	1,925	186	13	2	—	—	10,151	304	10,455
Performing	*4,114*	*3,740*	*1,865*	*174*	*11*	*1*	—	—	*9,905*	*297*	*10,202*
Non-performing	*71*	*100*	*60*	*12*	*2*	*1*	—	—	*246*	*7*	*253*

*unaudited

	2014							
	UK PBB £m	Ulster Bank RoI £m	Private Banking £m	RBS International £m	W&G £m	Total excluding Citizens £m	Citizens £m	Total £m
Mortgages	95,549	15,272	6,414	2,475	9,920	129,630	21,122	150,752
Of which:								
Interest only variable rate*	14,272	795	3,952	858	1,336	21,213	9,637	30,850
Interest only fixed rate*	8,193	8	1,520	27	946	10,694	292	10,986
Mixed (capital and interest only)*	6,163	120	—	—	741	7,024	788	7,812
Buy-to-let*	11,005	1,902	538	850	786	15,081	147	15,228
Forbearance stock: arrears status	4,350	3,857	51	49	546	8,853	409	9,262
Current	3,717	2,215	51	40	457	6,480	310	6,790
1-3 months in arrears	318	686	—	3	49	1,056	34	1,090
> 3 months in arrears	315	956	—	6	40	1,317	65	1,382
Provisions	216	1,378	7	20	36	1,657	146	1,803
REIL	1,144	3,270	22	73	166	4,675	949	5,624
Other lending	11,309	329	5,108	78	1,288	18,112	10,924	29,036
Total lending	106,858	15,601	11,522	2,553	11,208	147,742	32,046	179,788
Mortgage LTV ratios								
- Total portfolio	58%	93%	51%	51%	56%	61%	67%	62%
- New business	71%	77%	45%	56%	70%	68%	68%	68%
- Performing	58%	89%	51%	51%	56%	60%	67%	61%
- Non-performing	69%	115%	79%	81%	67%	93%	73%	91%

Mortgage LTV distribution

LTV ratio value 2014	<=50% £m	50% <=70% £m	70% <=90% £m	90% <=100% £m	100% <=110% £m	110% <=130% £m	130% <=150% £m	>150% £m	Total with LTVs £m	Other £m	Total £m
UK PBB	32,551	36,142	22,883	3,056	907	370	155	106	96,170	(621)	95,549
Performing	*32,163*	*35,436*	*22,247*	*2,885*	*832*	*322*	*143*	*88*	*94,116*	*(617)*	*93,499*
Non-performing	*388*	*706*	*636*	*171*	*75*	*48*	*12*	*18*	*2,054*	*(4)*	*2,050*
Ulster Bank RoI	2,331	2,135	2,650	1,309	1,336	2,688	1,973	850	15,272	—	15,272
Performing	*2,152*	*1,942*	*2,385*	*1,143*	*1,144*	*2,196*	*1,437*	*393*	*12,792*	*—*	*12,792*
Non-performing	*179*	*193*	*265*	*166*	*192*	*492*	*536*	*457*	*2,480*	*—*	*2,480*
Private Banking	2,768	2,684	745	43	29	10	4	16	6,299	115	6,414
Performing	*2,762*	*2,680*	*734*	*38*	*27*	*10*	*4*	*14*	*6,269*	*115*	*6,384*
Non-performing	*6*	*4*	*11*	*5*	*2*	*—*	*—*	*2*	*30*	*—*	*30*
RBS International	737	999	658	30	9	14	9	9	2,465	10	2,475
Performing	*729*	*989*	*645*	*26*	*6*	*5*	*8*	*8*	*2,416*	*9*	*2,425*
Non-performing	*8*	*10*	*13*	*4*	*3*	*9*	*1*	*1*	*49*	*1*	*50*
W&G	3,155	3,381	1,963	240	46	8	—	—	8,793	1,127	9,920
Performing	*3,104*	*3,293*	*1,883*	*215*	*37*	*7*	*—*	*—*	*8,539*	*1,094*	*9,633*
Non-performing	*51*	*88*	*80*	*25*	*9*	*1*	*—*	*—*	*254*	*33*	*287*

*unaudited

Credit risk: management basis continued

UK PBB*

Personal credit risk

Key credit portfolios

- The UK PBB personal mortgage portfolio increased by 10% to £104.8 billion. £90.7 billion (2014 - £84.5 billion) was owner-occupied and £14.1 billion (2014 - £11 billion) was buy-to-let. Of the total portfolio approximately £26 billion related to properties in the south east of England, while £20 billion related to properties in Greater London.
- Gross new mortgage lending amounted to £22.7 billion in 2015. Lending to owner-occupiers during this period was £18.9 billion (2014 - £15.5 billion) and had an average LTV by weighted value of 71% (2014 - 72%). Buy-to-let lending was £3.8 billion (2014 - £2.9 billion) with an average LTV by weighted value of 64% (2014 - 64%).
- Based on the Halifax House Price Index at September 2015, the portfolio average indexed LTV by volume was 49% (2014 - 51%) and 56% by weighted value of debt outstanding (2014 - 58%). This excludes £2 billion of mortgages granted by Ulster Bank Northern Ireland which are indexed against the house price index published by the Office of National Statistics.
- Of the total mortgage portfolio, approximately 60% (£63 billion) were fixed interest rate products of varying time durations with 2% (£2 billion) a combination of fixed and variable rates and the remainder variable rate. Approximately 15% (£13 billion) of owner-occupied mortgages were on interest-only terms with a bullet repayment and 6% (£5 billion) were on a combination of interest-only and capital and interest. The remainder were capital and interest. 65% (£9 billion) of the buy-to-let mortgages were on interest-only terms and 3% (£0.4 billion) on a combination of interest only and capital and interest.
- The arrears rate fell from 1.0% in December 2014 to 0.8% at the end of 2015. This reflected the growth in the mortgage portfolio, the stable UK economy and underlying asset quality.
- The flow of new forbearance was £273 million in the second half of 2015 compared with £367.5 million in the second half of 2014. The value of mortgages subject to forbearance has decreased by 16.8% since the previous year end to £3.6 billion (equivalent to 3.5% of the total mortgage book) as a result of improved market conditions and methodology changes.
- The majority (93%) of UK PBB forbearance is permanent in nature (term extensions, capitalisation of arrears, historic conversions to interest only). Temporary forbearance comprises payment concessions such as reduced or deferred payments with such arrangements typically agreed for a period of three to six months.
- The impairment charge for mortgage loans remained low at £2.8 million in 2015 reflecting continuing house price increases and is stable when compared to the net release of impairment provision of £29.5 million in 2014.
- A summary of the maturity profile for bullet principal repayment interest only mortgages (excluding mixed repayment mortgages) is set out below:*

The table below shows interest only mortgage portfolios (excluding mixed repayment mortgages) by type and by contractual year of maturity.

2015	2016 (1) £m	2017-18 £m	2019-23 £m	2024-28 £m	2029-33 £m	2034-43 £m	After 2043 £m	Total £m
Bullet principal repayment (2)	465	1,039	3,426	5,018	6,387	5,753	349	22,437
Conversion to amortising (2,3)	4	—	—	—	—	—	—	4
Total	469	1,039	3,426	5,018	6,387	5,753	349	22,441

2014	2015 (4) £m	2016-17 £m	2018-22 £m	2023-27 £m	2028-32 £m	2033-42 £m	After 2042 £m	Total £m
Bullet principal repayment (2)	475	1,007	3,520	4,825	6,474	5,855	294	22,450
Conversion to amortising (2,3)	14	1	—	—	—	—	—	15
Total	489	1,008	3,520	4,825	6,474	5,855	294	22,465

Notes:
(1) 2016 includes pre-2016 maturity exposure.
(2) Includes £1.5 billion (2014 - £1.6 billion) of repayment mortgages that have been granted interest only concessions (forbearance).
(3) Maturity date relates to the expiry of the interest only period.
(4) 2015 includes pre-2015 maturity exposure.

*unaudited

Ulster Bank RoI*

Overview

- Ulster Bank RoI's residential mortgage portfolio totalled £13.8 billion at 31 December 2015. Excluding the impact of exchange rate movements, the portfolio decreased by 4.4% from 31 December 2014 as a result of amortisation - a portion of which related to the variable rate mortgage portfolio and the sale of a £0.3 billion buy-to-let mortgage portfolio. The volume of new business has increased reflecting continuing market demand.
- Gross new mortgage lending amounted to £522 million in 2015. Lending to owner-occupiers during this period was £511 million (2014 - £392 million) and had an average LTV by weighted value of 77% (2014 - 76%). Buy-to-let lending was £10 million (2014 - £10 million) with an average LTV by weighted value of 66% (2014 - 73%).
- The interest-rate product mix was approximately 87% (£12.0 billion) of the mortgage portfolio on variable-rate products and 13% (£1.7 billion) on fixed rate.
- The portfolio average indexed LTV decreased from 93% at 31 December 2014 to 83% at 31 December 2015 as a result of improved market conditions and the sale of a buy-to-let mortgage portfolio.
- At 31 December 2015, 26% of total mortgage assets (£3.5 billion) were subject to a forbearance arrangement, a decrease of 9% (£0.3 billion) from 31 December 2014. Excluding the impact of exchange rate movements, the value of mortgage assets subject to a forbearance arrangement has decreased by £131 million (3.3%).
- The number of customers approaching Ulster Bank RoI for the first time in respect of forbearance assistance declined through 2015.
- A total of 59% (£2.1 billion) of forborne loans were subject to a long term arrangement (capitalisations, term extensions, economic concessions) at 31 December 2015 (2014 - 51%, £2.0 billion). Short term forbearance comprises payment concessions, amortising payments of outstanding balances, payment holidays and temporary interest only arrangements.
- The impairment release was driven by a decrease in defaulted assets leading to reduced loss expectations.
- Ulster Bank RoI stopped offering interest only loans as a standard mortgage offering for new lending in the Republic of Ireland in 2010. Interest only mortgages are now granted only to customers in need of forbearance. A summary of the maturity profile for bullet principal repayment interest only mortgages (excluding mixed repayment mortgages) is set out below:*

The table below shows interest only mortgage portfolios (excluding mixed repayment mortgages) by type and by contractual year of maturity.

2015	2016 (1) £m	2017-18 £m	2019-23 £m	2024-28 £m	2029-33 £m	2034-43 £m	After 2043 £m	Total £m
Bullet principal repayment (2)	7	14	28	44	67	26	6	192
Conversion to amortising (2,3)	308	119	5	3	3	2	1	441
Total	315	133	33	47	70	28	7	633

2014	2015 (4) £m	2016-17 £m	2018-22 £m	2023-27 £m	2028-32 £m	2033-42 £m	After 2042 £m	Total £m
Bullet principal repayment (2)	6	16	32	45	69	35	8	211
Conversion to amortising (2,3)	352	205	29	2	4	—	—	592
Total	358	221	61	47	73	35	8	803

Notes:
(1) 2016 includes pre-2016 maturity exposure.
(2) Includes £0.1 billion (2014 - £0.3 billion) of repayment mortgages that have been granted interest only concessions (forbearance).
(3) Maturity date relates to the expiry of the interest only period.
(4) 2015 includes pre-2015 maturity exposure.

*unaudited

Credit risk: management basis continued

Private Banking*

Overview

- The majority of the Private Banking personal lending portfolio relates to mortgage lending. The portfolio increased by 3% during 2015.
- Gross new mortgage lending amounted to £2.4 billion in 2015. Lending to owner-occupiers during this period was £2.2 billion (2014 - £2.4 billion) with an average LTV by weighted value of 54% (2014 - 57%). Buy-to-let lending was £0.2 billion (2014 - £0.2 billion) with an average LTV by weighted value of 64% (2014 - 59%).
- The number of customers with mortgages in forbearance at the end of 2015 increased from 43 to 59 compared to the end of 2014. In value terms, the exposure increased from £51 million to £64 million.
- A total of 85% (£54 million) of forbearance loans were subject to a long term arrangement (capitalisations, term extensions, economic concessions) at 31 December 2015 (2014 - 65% or £32.8 million). Short term forbearance comprises payment concessions, amortising payments of outstanding balances, payment holidays and temporary interest only arrangements.
- Private Banking offers interest-only mortgages to high net worth customers, with over a third of the book typically being refinanced/replaced per annum. A summary of the maturity profile for bullet principal repayment interest only mortgages (excluding mixed repayment mortgages) is set out below.

The table below shows interest only mortgage portfolios (excluding mixed repayment mortgages) by type and by contractual year of maturity.

2015	2016 (1) £m	2017-18 £m	2019-23 £m	2024-28 £m	2029-33 £m	2034-43 £m	After 2043 £m	Total £m
Bullet principal repayment	1,004	1,532	1,603	830	286	202	2	5,459

2014	2015 (2) £m	2016-17 £m	2018-22 £m	2023-27 £m	2028-32 £m	2033-42 £m	After 2042 £m	Total £m
Bullet principal repayment	1,231	1,452	2,060	444	171	113	1	5,472

Notes:
(1) 2016 includes pre-2016 maturity exposure.
(2) 2015 includes pre-2015 maturity exposure.

RBS International*

Overview

- The majority (98%) of RBSI's personal lending is mortgage lending. The mortgage portfolio increased by 3% to £2.5 billion.
- Gross new mortgage lending amounted to £0.2 billion in 2015. Lending to owner-occupiers during this period was £0.2 billion (2014 - £0.2 billion) and had an average LTV by weighted value of 66% (2014 - 66%). Buy-to-let lending was £0.1 billion (2014 - £0.1 billion) with an average LTV by weighted value of 59% (2014 - 60%).
- The number of customers granted forbearance in 2015 decreased by 10%.
- A total of £12 million of forborne loans were subject to a long-term arrangement (term extensions) at 31 December 2015 (2014 - £13 million). Short term forbearance comprises covenant breaches, payment suspensions and reduced payments.
- RBSI offers interest only mortgages for buy-to-let. A summary of the maturity profile for bullet principal repayment interest only mortgages (excluding mixed repayment mortgages) is set out below:*

2015	2016 (1) £m	2017-18 £m	2019-23 £m	2024-28 £m	2029-33 £m	2034-43 £m	After 2043 £m	Total £m
Bullet principal repayment	83	182	157	183	146	39	1	791

2014	2015 (2) £m	2016-17 £m	2018-22 £m	2023-27 £m	2028-32 £m	2033-42 £m	After 2042 £m	Total £m
Bullet principal repayment	59	182	224	186	185	49	—	885

Notes:
(1) 2016 includes pre-2016 maturity exposure.
(2) 2015 includes pre-2015 maturity exposure.

*unaudited

Williams & Glyn*

Overview

The retail mortgage portfolio increased by 5.4% to £10.5 billion, of which £9.3 billion (2014 - £9.2 billion) was owner-occupied and £1.2 billion (2014 - £0.8 billion) was buy-to-let.

Gross new mortgage lending amounted to £1.7 billion in 2015. Lending to owner-occupiers during this period was £1.4 billion (2014 - £1.3 billion) and had an average LTV by weighted value of 70% (2014 - 71%). Buy-to-let lending was £0.3 billion (2014 - £0.2 billion) with an average LTV by weighted value of 64% (2014 - 64%).

Fixed interest rate products of varying time durations accounted for approximately 55% (£5.7 billion) of the mortgage portfolio with 7% (£0.8 billion) a combination of fixed and variable rates and the remainder (£4 billion) variable rate.

The arrears rate fell to 1.1% at 31 December 2015 (2014 - 1.3%). This reflected improvements in the UK economy and underlying asset quality.

The flow of new forbearance was £59.4 million in 2015 compared to £82.5 million in 2014. The value of mortgages subject to forbearance decreased by 5% in 2015 to £0.52 billion (equivalent to 5% of the total mortgage portfolio) as a result of improved market conditions and methodology changes.

There was a reduction of impairment provision balances for personal mortgages in 2015 to £25.6 million compared with £35.6 million in 2014. The provision release resulted from lower LGDs and a decrease in forborne mortgages.

2015	2016 (1) £m	2017-18 £m	2019-23 £m	2024-28 £m	2029-33 £m	2034-43 £m	After 2043 £m	Total £m
Bullet principal repayment (2)	58	124	421	625	675	539	35	2,477

2014	2015 (3) £m	2016-17 £m	2018-22 £m	2023-27 £m	2028-32 £m	2033-42 £m	After 2042 £m	Total £m
Bullet principal repayment (2)	31	93	381	540	671	539	27	2,282

Notes:
(1) 2015 includes pre-2015 maturity exposure.
(2) Includes £0.2 billion (2014 - £0.2 billion) of repayment mortgages that have been granted interest only concessions (forbearance).
(3) 2014 includes pre-2014 maturity exposure.

*unaudited

Credit risk: management basis continued

Country risk

Risk measurement*

In this section, country exposure includes wholesale and retail net on-balance sheet exposure (drawn amounts under lending facilities, net of provisions, mark-to-market derivatives positions and issuer-risk debt securities positions in the banking book and trading book) together with off-balance sheet exposure (contingent obligations and undrawn commitments).

Basis of preparation*

The tables in this section show RBS plc's exposure at 31 December 2015 and 2014. Exposures are reported by country of operation of the obligor, except exposures to governments and individuals, which are shown by country of residence.

The country of operation is the counterparty's country of main operations, taking account of branches and subsidiaries.

Countries shown are those which had ratings of A+ or below from Standard and Poor's, Moody's or Fitch at 31 December 2015, and in which RBS plc's net balance sheet exposure to counterparties operating (or individuals residing) in them exceeded £1 billion. Selected eurozone countries are also included.

The exposures are stated before taking into account risk mitigants such as guarantees, insurance or collateral (with the exception of reverse repos) which may have been put in place to reduce or eliminate exposure to country risk events. The tables separately show CDS positions, as RBS plc may be either a net buyer or a net seller of protection.

Exposures relating to ocean-going vessels are not included as they cannot be meaningfully assigned to specific countries from a country risk perspective.

Overview

The comments below relate to changes in country exposures in 2015 unless indicated otherwise*.

- Net balance sheet and off-balance sheet exposure to most countries and products declined. RBS continued to maintain a cautious stance and implemented its strategy to become a more UK-centred bank with an international focus on Western Europe. In addition, many clients continued to reduce debt levels. The euro depreciated against sterling by 5.7% while the US dollar appreciated by 5.3%.
- Total eurozone net balance sheet exposure decreased by £8.0 billion or 8%, to £86.3 billion. The depreciation of the euro played a significant role in the reduction.
- Eurozone periphery: Ireland is no longer considered part of this group because of its improved economic conditions. The remaining exposure to the eurozone periphery is relatively small.
- Italy - exposure fell by £0.9 billion to £2.5 billion. This was the result of the maturity of a few large derivatives transactions with banks, and of reductions in corporate lending.
- Spain - exposure decreased by £1.1 billion to £2.1 billion. This largely reflected reductions in corporate lending (mostly to the commercial real estate, construction and land transport sectors).
- Portugal - exposure decreased by £0.1 billion to £0.6 billion, due largely to decreases in derivatives exposure to banks and corporate clients.
- Greece - net balance sheet exposure decreased to £0.1 billion (from £0.4 billion), mostly as a result of sales of derivatives positions. The remaining exposure was mostly lending and collateralised derivatives exposure to corporates, including subsidiaries of international clients.
- Germany - net balance sheet exposure increased by £5.9 billion to £32.3 billion. This was the net result of an increase of £14.0 billion in cash deposits with the central bank, driven by RBS Treasury's global liquidity management, against reductions in other areas, notably in net HFT bonds.
- Ireland - exposure fell by £3.0 billion or 13% to £19.6 billion, with exposure to corporates and households (mostly mortgage lending) decreasing by £1.9 billion and £1.4 billion respectively. This largely reflected currency movements and portfolio sales. The latter also drove a £5.6 billion reduction in lending provisions and a £1.0 billion increase in Ulster Bank RoI's cash deposits with the central bank.
- France - net balance sheet exposure fell by £4.0 billion to £11.9 billion, with reductions mainly in net HFT bonds and lending to banks. Available-for-sale (AFS) bonds rose by £0.7 billion, as part of the bank's liquidity management.
- Netherlands - net balance sheet exposure decreased by £3.7 billion, the result of reductions in derivatives, lending, AFS bonds, and in net HFT exposure.
- Japan - net HFT bonds exposure increased by £4.1 billion to £7.2 billion, driven by collateral trading in London. This increase in holdings reflects reduced access to local repo markets following RBS's decision to exit its Japanese onshore business. Derivatives exposure, largely to banks, decreased by £0.6 billion.
- Russia - net balance sheet exposure decreased by £1.4 billion to £0.4 billion, partly through loan sales in the second half of 2015. The remaining exposure was below the £1 billion threshold for inclusion in the table. It was on run-off, and consisted mainly of lending to banks and with

*unaudited

Summary of country exposures

2015	Net balance sheet exposure: Banks: Sovereign £m	Banks: & other FI £m	Banks: Corporate £m	Banks: Personal £m	Banks: Total £m	Analysis of net balance sheet exposures: Net lending £m	Debt securities: AFS/LAR £m	Debt securities: HFT (net) £m	Net: Derivatives £m	Net: SFT £m	Off-balance sheet £m	Total exposure £m	CDS notional less fair value £m	Gross: Derivatives £m	Gross: SFT £m
Eurozone periphery															
Italy	1,152	1,017	316	27	2,512	341	5	1,105	1,061	—	1,240	3,752	(411)	5,030	1,274
Spain	289	428	1,345	79	2,141	1,287	—	268	584	2	1,407	3,548	(224)	2,853	323
Portugal	211	204	215	6	636	264	—	203	169	—	172	808	(57)	196	188
Greece	—	1	56	15	72	33	—	—	39	—	14	86	(36)	39	—
Cyprus	—	—	43	13	56	41	—	—	15	—	10	66	—	15	—
Eurozone other															
Germany	23,148	7,615	1,500	63	32,326	17,767	7,822	(871)	7,523	85	4,333	36,659	(2,027)	28,707	2,535
Ireland	1,727	929	3,761	13,181	19,598	18,600	12	377	609	—	2,294	21,892	(14)	1,808	714
France	3,968	6,673	1,177	76	11,894	1,847	2,439	1,594	5,943	71	7,228	19,122	(1,779)	30,445	17,807
Netherl.	1,368	7,162	1,076	30	9,636	1,829	734	2,050	5,015	8	4,626	14,262	(423)	14,582	1,790
Belgium	459	2,393	263	22	3,137	393	473	(42)	1,898	415	870	4,007	(119)	2,409	1,644
Luxemb.	21	1,148	755	6	1,930	982	428	30	227	263	1,045	2,975	(33)	337	3,754
Other	1,236	796	283	14	2,329	518	311	577	923	—	746	3,075	(498)	3,579	185
Eurozone	33,579	28,366	10,790	13,532	86,267	43,902	12,224	5,291	24,006	844	23,985	110,252	(5,621)	90,000	30,214
Japan	8,593	1,978	40	31	10,642	1,667	—	7,174	1,797	4	191	10,833	(26)	8,224	2,218
2014															
Eurozone periphery															
Italy	22	2,209	1,186	25	3,442	987	44	5	2,406	—	2,031	5,473	(472)	8,641	823
Spain	210	747	2,182	88	3,227	2,022	6	364	835	—	1,920	5,147	(310)	3,913	422
Portugal	111	310	319	8	748	282	20	152	294	—	222	970	(155)	338	613
Greece	8	259	92	17	376	63	—	8	305	—	23	399	(8)	416	—
Cyprus	—	—	80	14	94	75	—	—	19	—	16	110	—	19	—
Eurozone other															
Germany	14,872	9,411	2,041	86	26,410	4,562	6,992	5,653	8,308	895	6,008	32,418	(1,736)	39,262	8,547
Ireland	826	1,565	5,611	14,593	22,595	21,134	56	413	991	1	2,913	25,508	(48)	2,135	1,464
France	5,008	9,009	1,764	81	15,862	2,930	1,743	4,034	6,389	766	8,471	24,333	(2,384)	41,094	17,442
Netherl.	330	10,917	2,082	29	13,358	2,831	1,493	2,509	6,441	84	6,155	19,513	(798)	20,588	3,573
Belgium	554	2,303	389	21	3,267	566	15	375	2,227	84	855	4,122	(218)	3,264	932
Luxemb.	18	1,199	781	5	2,003	966	329	70	461	177	1,475	3,478	(52)	696	2,628
Other	1,540	806	533	16	2,895	612	200	930	1,148	5	1,047	3,942	(560)	4,818	302
Eurozone	23,499	38,735	17,060	14,983	94,277	37,030	10,898	14,513	29,824	2,012	31,136	125,413	(6,741)	125,184	36,746
Japan	4,264	2,403	322	33	7,022	1,595	—	3,043	2,359	26	842	7,865	(25)	10,129	10,005

Notes:
(1) Net balance sheet exposure - Comprises net lending, debt securities, derivatives (net) and SFT (net) exposures, as defined below.
(2) Net lending - Comprises loans and advances net of provisions and includes cash balances.
(3) Debt securities - includes held-for-trading (HFT), designated as fair value through profit or loss (DFV), available for-for-sale (AFS) and loans and receivables (LAR). HFT debt securities, aggregated with DFV securities, are presented as long positions net of short positions.
(4) Derivatives (net) - Comprise the mark-to-market (mtm) value of such contracts after the effect of legally enforceable netting agreements in line with regulatory capital models, but before the effect of collateral.
(5) Securities financing transactions (SFT) (net) - Comprise the mtm value of the cash and securities that are due to RBS at a future date after the effect of collateral intrinsic to the transaction and legally enforceable netting agreements. Counterparty netting is applied in line with regulatory capital approach. Additional collateral called to offset mtm positions (variation margin) is not included.
(6) Off-balance sheet - Comprises letters of credit, guarantees, other contingent obligations and legally committed undrawn facilities.
(7) Total exposure - Comprises net balance sheet exposure and off-balance sheet exposure, as defined above.
(8) Credit default swaps (CDSs) - Under a CDS contract, the credit risk on the reference entity is transferred from the buyer to the seller. 'Fair value' (or 'mtm value') represents the balance sheet carrying value of the resulting exposure. The mtm value of CDSs is included in derivatives against the counterparty of the trade, as opposed to the reference entity. The notional is the par value of the credit protection bought or sold and is included against the reference entity of the CDS contract. The column 'CDS notional less fair value' represents the net effect on exposure should the CDS contracts be triggered by a credit event, assuming a zero recovery rate on the reference exposure. This net effect would be the increase in exposure arising from sold positions netted against the decrease arising from bought positions. For a sold position, the change in exposure equals the notional less the fair value amount; this represents the amount RBS would owe to its CDS counterparties if the reference entity defaulted. Positive recovery rates would tend to reduce the gross components (increases and decreases) of those numbers.
(9) Other eurozone - Austria, Estonia, Finland, Latvia, Malta, Slovakia and Slovenia.

Credit risk: balance sheet analysis

Credit risk assets analysed on pages 73 to 95 are reported internally to senior management. However they exclude certain exposures, primarily securities and reverse repurchase agreements and take account of legal netting agreements, that provide a right if legal set-off but do not meet the offset criteria in IFRS. The tables that follow are therefore provided to supplement disclosures of credit risk assets to reconcile to the balance sheet. All the disclosures in this section are audited.

Financial assets

Exposure summary and credit mitigation

The following table analyses the Group's financial asset exposures, both gross and net of offset arrangements.

	Group				
2015	Gross exposure £m	IFRS offset (1) £m	Carrying value (2) £m	Balance sheet offset (3) £m	Exposure post offset £m
Cash and balances at central banks	78,999	—	78,999	—	78,999
Reverse repos	74,171	(34,361)	39,810	(2,499)	37,311
Lending	325,129	(2,955)	322,174	(35,568)	286,606
Debt securities	80,027	—	80,027	—	80,027
Equity shares	1,069	—	1,069	—	1,069
Derivatives	385,470	(123,662)	261,808	(242,404)	19,404
Settlement balances	5,314	(1,225)	4,089	(26)	4,063
Total third party excluding disposal groups	950,179	(162,203)	787,976	(280,497)	507,479
Disposal groups	3,356	—	3,356	—	3,356
Total third party including disposal groups	953,535	(162,203)	791,332	(280,497)	510,835
Amounts due from holding company and fellow subsidiaries	4,109	—	4,109	(393)	3,716
Total gross of short positions	957,644	(162,203)	795,441	(280,890)	514,551
Short positions	(20,808)	—	(20,808)	—	(20,808)
Total net of short positions	936,836	(162,203)	774,633	(280,890)	493,743
2014					
Cash and balances at central banks	73,983	—	73,983	—	73,983
Reverse repos	95,517	(30,822)	64,695	(5,016)	59,679
Lending	356,100	(2,921)	353,179	(40,011)	313,168
Debt securities	84,274	—	84,274	—	84,274
Equity shares	5,203	—	5,203	—	5,203
Derivatives	597,262	(245,418)	351,844	(327,807)	24,037
Settlement balances	6,662	(1,997)	4,665	—	4,665
Total third party excluding disposal groups	1,219,001	(281,158)	937,843	(372,834)	565,009
Disposal groups	78,240	—	78,240	—	78,240
Total third party including disposal groups	1,297,241	(281,158)	1,016,083	(372,834)	643,249
Amounts due from holding company and fellow subsidiaries	6,440	—	6,440	(979)	5,461
Total gross of short positions	1,303,681	(281,158)	1,022,523	(373,813)	648,710
Short positions	(23,028)	—	(23,028)	—	(23,028)
Total net of short positions	1,280,653	(281,158)	999,495	(373,813)	625,682

For the notes to this table refer to the following page.

The table below analyses the Bank's financial asset exposures, both gross and net of offset arrangements.

	Bank				
2015	Gross exposure £m	IFRS offset (1) £m	Carrying value (2) £m	Balance sheet offset (3) £m	Exposure post offset £m
Cash and balances at central banks	76,904	—	76,904	—	76,904
Reverse repos	47,285	(20,374)	26,911	(2,050)	24,861
Lending	130,672	(2,955)	127,717	(28,634)	99,083
Debt securities	72,894	—	72,894	—	72,894
Equity shares	931	—	931	—	931
Derivatives	384,537	(123,662)	260,875	(242,232)	18,643
Settlement balances	2,796	(168)	2,628	—	2,628
Total third party	716,019	(147,159)	568,860	(272,916)	295,944
Amounts due from holding company and fellow subsidiaries	61,233	—	61,233	(1,963)	59,270
Total gross of short positions	777,252	(147,159)	630,093	(274,879)	355,214
Short positions	(17,593)	—	(17,593)	—	(17,593)
Total net of short positions	759,659	(147,159)	612,500	(274,879)	337,621
2014					
Cash and balances at central banks	70,952	—	70,952	—	70,952
Reverse repos	61,717	(14,951)	46,766	(4,751)	42,015
Lending	162,798	(2,921)	159,877	(33,149)	126,728
Debt securities	70,898	—	70,898	—	70,898
Equity shares	4,880	—	4,880	—	4,880
Derivatives	595,970	(245,413)	350,557	(327,548)	23,009
Settlement balances	3,029	(156)	2,873	—	2,873
Total third party	970,244	(263,441)	706,803	(365,448)	341,355
Amounts due from holding company and fellow subsidiaries	92,507	—	92,507	(4,998)	87,509
Total gross of short positions	1,062,751	(263,441)	799,310	(370,446)	428,864
Short positions	(16,590)	—	(16,590)	—	(16,590)
Total net of short positions	1,046,161	(263,441)	782,720	(370,446)	412,274

Notes:
(1) Relates to offset arrangements that comply with IFRS criteria and transactions cleared through and novated to central clearing houses, primarily London Clearing House.
(2) The amount by which credit risk exposure is reduced through arrangements, such as master netting agreements and cash management pooling, which give the Group a legal right to set off the financial asset against a financial liability due to the same counterparty.
(3) The Group holds collateral in respect of net exposures above. For individual loans and advances to banks and customers, this collateral includes mortgages over property (both personal and commercial); charges over business assets such as plant, inventories and trade debtors; and guarantees of lending from parties other than the borrower. The Group obtains collateral in the form of securities in reverse repurchase agreements. Cash and securities are received as collateral in respect of derivative transactions.

Key points

- Total third party exposure post offset excluding disposal groups decreased by £58 billion, principally reflecting lower funded assets as both CIB and Capital Resolution implemented strategic balance sheet reductions through disposals and wind-downs.
- Part of the lending exposure is secured by property collateral, £137 billion (2014 - £130 billion) by residential property and £27 billion (2014 - £43 billion) by commercial real estate.
- Of the debt securities of £80 billion (2014 - £84 billion), 83% (2014 - 74%) was issued by central and local governments and £5 billion comprised asset-backed securities.
- Derivatives net exposure is additionally covered by £8 billion of securities collateral.

Credit risk: balance sheet analysis continued

Sector concentration

The following tables analyse financial assets by industry sector.

	Group								
			Securities						
2015	Reverse repos £m	Lending £m	Debt £m	Equity £m	Derivatives £m	Other financial assets £m	Balance sheet value £m	Offset £m	Exposure post offset £m
Central and local government	362	6,670	66,535	—	3,286	126	76,979	(6,346)	70,633
Financial institutions - banks	11,098	17,188	2,215	40	169,403	78,999	278,943	(177,778)	101,165
- other	28,094	31,375	10,539	712	78,168	3,750	152,638	(84,992)	67,646
Personal - mortgages	—	137,465	—	—	—	—	137,465	—	137,465
- unsecured	—	15,120	—	—	33	—	15,153	—	15,153
Property	—	35,720	124	47	1,336	—	37,227	(1,084)	36,143
Construction	—	4,411	—	3	240	—	4,654	(932)	3,722
Manufacturing	184	9,645	128	160	1,931	94	12,142	(1,593)	10,549
Finance leases and instalment credit	—	11,435	1	—	10	—	11,446	(2)	11,444
Retail, wholesale and repairs	—	12,000	156	31	570	10	12,767	(1,329)	11,438
Transport and storage	—	8,804	87	2	1,362	—	10,255	(873)	9,382
Health, education and leisure	—	10,959	4	6	641	7	11,617	(690)	10,927
Hotels and restaurants	—	5,363	11	—	81	5	5,460	(232)	5,228
Utilities	—	3,392	47	19	3,267	—	6,725	(1,689)	5,036
Other	72	19,679	237	111	1,480	97	21,676	(2,957)	18,719
Total third party	39,810	329,226	80,084	1,131	261,808	83,088	795,147	(280,497)	514,650
Amounts due from holding company and fellow subsidiaries	—	2,815	—	—	1,275	19	4,109	(393)	3,716
Total gross of provisions	39,810	332,041	80,084	1,131	263,083	83,107	799,256	(280,890)	518,366
Provisions	—	(7,052)	(57)	(62)	—	—	(7,171)	n/a	(7,171)
Total excluding disposal groups	39,810	324,989	80,027	1,069	263,083	83,107	792,085	(280,890)	511,195
Disposal groups	67	2,281	419	24	30	535	3,356	—	3,356
Total	39,877	327,270	80,446	1,093	263,113	83,642	795,441	(280,890)	514,551
2014									
Central and local government	10	8,472	62,361	—	4,832	251	75,926	(5,041)	70,885
Financial institutions - banks	20,708	21,591	4,846	373	239,408	73,983	360,909	(247,477)	113,432
- other	43,682	37,660	14,904	1,253	92,442	4,284	194,225	(108,898)	85,327
Personal - mortgages	—	129,671	—	—	—	—	129,671	—	129,671
- unsecured	—	17,980	—	—	—	2	17,982	(3)	17,979
Property	—	46,507	165	101	2,347	8	49,128	(903)	48,225
Construction	—	5,287	11	53	366	—	5,717	(896)	4,821
Manufacturing	265	15,696	665	1,602	2,149	48	20,425	(2,024)	18,401
Finance leases and instalment credit	—	11,265	21	—	26	—	11,312	(1)	11,311
Retail, wholesale and repairs	—	15,582	252	438	733	13	17,018	(1,735)	15,283
Transport and storage	—	13,120	214	57	2,116	—	15,507	(1,027)	14,480
Health, education and leisure	—	12,392	59	25	670	—	13,146	(709)	12,437
Hotels and restaurants	—	6,084	4	37	180	—	6,305	(198)	6,107
Utilities	—	4,516	242	127	4,330	—	9,215	(1,150)	8,065
Other	30	24,760	631	1,204	2,245	59	28,929	(2,772)	26,157
Total third party	64,695	370,583	84,375	5,270	351,844	78,648	955,415	(372,834)	582,581
Amounts due from holding company and fellow subsidiaries	—	3,657	—	—	2,738	45	6,440	(979)	5,461
Total gross of provisions	64,695	374,240	84,375	5,270	354,582	78,693	961,855	(373,813)	588,042
Provisions	—	(17,404)	(101)	(67)	—	—	(17,572)	n/a	(17,572)
Total excluding disposal groups	64,695	356,836	84,274	5,203	354,582	78,693	944,283	(373,813)	570,470
Disposal groups	—	61,351	15,293	572	402	622	78,240	—	78,240
Total	64,695	418,187	99,567	5,775	354,984	79,315	1,022,523	(373,813)	648,710

2015	Bank								
	Reverse repos £m	Lending £m	Securities: Debt £m	Securities: Equity £m	Derivatives £m	Other financial assets £m	Balance sheet value £m	Offset £m	Exposure post offset £m
Central and local government	—	4,994	60,982	—	3,284	20	69,280	(5,152)	64,128
Financial institutions - banks	8,724	12,536	1,880	40	169,354	76,904	269,438	(177,777)	91,661
- other	17,956	25,128	9,341	583	77,923	2,441	133,372	(83,411)	49,961
Personal - mortgages	—	30,697	—	—	—	—	30,697	—	30,697
- unsecured	—	3,373	—	—	—	—	3,373	—	3,373
Property	—	17,921	124	18	1,078	—	19,141	(807)	18,334
Construction	—	1,766	—	2	238	—	2,006	(111)	1,895
Manufacturing	184	4,346	128	157	1,897	73	6,785	(1,196)	5,589
Finance leases and instalment credit	—	103	1	—	10	—	114	(2)	112
Retail, wholesale and repairs	—	3,984	156	31	550	5	4,726	(668)	4,058
Transport and storage	—	6,842	87	2	1,351	—	8,282	(635)	7,647
Health, education and leisure	—	4,761	4	2	470	7	5,244	(205)	5,039
Hotels and restaurants	—	2,331	11	—	63	5	2,410	(114)	2,296
Utilities	—	2,623	47	19	3,215	—	5,904	(1,443)	4,461
Other	47	7,836	190	100	1,442	77	9,692	(1,395)	8,297
Total third party	26,911	129,241	72,951	954	260,875	79,532	570,464	(272,916)	297,548
Amounts due from holding company and fellow subsidiaries	—	52,374	3,708	—	4,726	425	61,233	(1,963)	59,270
Total gross of provisions	26,911	181,615	76,659	954	265,601	79,957	631,697	(274,879)	356,818
Provisions	—	(1,524)	(57)	(23)	—	—	(1,604)	n/a	(1,604)
Total	26,911	180,091	76,602	931	265,601	79,957	630,093	(274,879)	355,214

2014									
Central and local government	—	6,957	53,322	—	4,829	14	65,122	(4,013)	61,109
Financial institutions - banks	14,821	15,281	4,018	371	239,331	70,952	344,774	(247,475)	97,299
- other	31,650	31,535	11,827	1,121	92,143	2,809	171,085	(107,580)	63,505
Personal - mortgages	—	32,817	—	—	—	—	32,817	—	32,817
- unsecured	—	3,811	—	—	—	—	3,811	(3)	3,808
Property	—	19,928	164	70	1,973	3	22,138	(595)	21,543
Construction	—	2,476	9	53	363	—	2,901	(150)	2,751
Manufacturing	265	9,798	517	1,599	2,104	37	14,320	(1,525)	12,795
Finance leases and instalment credit	—	134	10	—	26	—	170	(1)	169
Retail, wholesale and repairs	—	6,523	217	438	689	10	7,877	(781)	7,096
Transport and storage	—	10,623	189	52	2,095	—	12,959	(813)	12,146
Health, education and leisure	—	5,492	45	25	481	—	6,043	(157)	5,886
Hotels and restaurants	—	2,644	4	17	135	—	2,800	(56)	2,744
Utilities	—	3,793	230	127	4,245	—	8,395	(951)	7,444
Other	30	11,529	447	1,030	2,143	—	15,179	(1,348)	13,831
Total third-party	46,766	163,341	70,999	4,903	350,557	73,825	710,391	(365,448)	344,943
Amounts due from holding company and fellow subsidiaries	—	66,035	16,696	—	9,268	508	92,507	(4,998)	87,509
Total gross of provisions	46,766	229,376	87,695	4,903	359,825	74,333	802,898	(370,446)	432,452
Provisions	—	(3,464)	(101)	(23)	—	—	(3,588)	n/a	(3,588)
Total	46,766	225,912	87,594	4,880	359,825	74,333	799,310	(370,446)	428,864

For geographic concentrations refer to:

- Lending: Loans and related credit metrics;
- Debt securities: IFRS measurement and issue and Credit risk - Country risk; and
- Equity shares.

Credit risk: balance sheet analysis continued

Asset quality

The asset quality analysis presented below is based on the Group's internal asset quality ratings which have ranges for the probability of default. Customers are assigned credit grades, based on various credit grading models that reflect the key drivers of default for the customer type. All credit grades across the Group map to both an asset quality scale, used for external financial reporting, and a master grading scale for wholesale exposures used for internal management reporting across portfolios. Debt securities are analysed by external ratings and are therefore excluded from the following table and are set out on pages 112 to 115.

The table that follows details the relationship between the Group's master grading scale and AQ bands and external ratings published by Standard & Poor's (S&P) for illustrative purposes only. This relationship is established by observing S&P's default study statistics, notably the one year default rates for each S&P rating grade. A degree of judgement is required to relate the PD ranges associated with the master grading scale to these default rates given that, for example, the S&P published default rates do not increase uniformly by grade and the historical default rate is nil for the highest rating categories.

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

The mapping to the S&P ratings is used by the Group as one of several benchmarks for its wholesale portfolios, depending on customer type and the purpose of the benchmark. The mapping is based on all issuer types rated by S&P. It should therefore be considered illustrative and does not, for instance, indicate that exposures reported against S&P ratings either have been or would be assigned those ratings if assessed by S&P. In addition, the relationship is not relevant for retail portfolios, smaller corporate exposures or specialist corporate segments given that S&P does not typically assign ratings to such entities.

	Group														
2015	AQ1 £bn	AQ2 £bn	AQ3 £bn	AQ4 £bn	AQ5 £bn	AQ6 £bn	AQ7 £bn	AQ8 £bn	AQ9 £bn	AQ10 £bn	Balances with holding company and fellow subsidiaries £bn	Past due £bn	Impaired £bn	Impairment provisions £bn	Total £bn
Cash and balances at central banks	76.9	—	2.1	—	—	—	—	—	—	—	—	—	—	—	79.0
Banks															
- Reverse repos	0.3	0.6	3.5	4.8	1.3	0.4	0.2	—	—	—	—	—	—	—	11.1
- Derivative cash collateral	3.6	4.6	1.4	1.2	0.2	—	—	—	—	—	—	—	—	—	11.0
- Bank loans	2.0	0.6	2.7	0.1	0.3	0.1	0.1	—	0.1	—	1.6	0.1	—	—	7.7
- Total	5.9	5.8	7.6	6.1	1.8	0.5	0.3	—	0.1	—	1.6	0.1	—	—	29.8
Customers															
- Reverse repos	21.9	0.4	1.5	3.1	1.7	0.1	—	—	—	—	—	—	—	—	28.7
- Derivative cash collateral	9.2	1.1	3.6	3.0	0.2	0.1	—	—	—	—	—	—	—	—	17.2
- Customer loans	22.9	12.0	28.7	105.5	51.2	29.2	20.2	4.1	2.6	1.1	1.2	6.7	10.7	(7.1)	289.0
- Total	54.0	13.5	33.8	111.6	53.1	29.4	20.2	4.1	2.6	1.1	1.2	6.7	10.7	(7.1)	334.9
Settlement balances and other financial assets	2.3	0.1	0.1	0.6	—	—	—	—	—	—	—	1.0	—	—	4.1
Derivatives	41.4	65.6	88.9	57.5	6.2	1.1	0.8	—	0.2	0.1	1.3	—	—	—	263.1
Undrawn commitments	24.1	6.9	20.1	41.7	27.6	8.7	7.0	0.6	0.2	0.5	—	—	—	—	137.4
Contingent liabilities	0.8	1.3	1.8	4.4	1.9	0.6	0.9	0.1	0.1	0.1	0.7	—	—	—	12.7
Total excluding disposal groups	205.4	93.2	154.4	221.9	90.6	40.3	29.2	4.8	3.2	1.8	4.8	7.8	10.7	(7.1)	861.0
Disposal groups															2.9
Total															863.9
Total %	23.8	10.8	17.9	25.8	10.5	4.7	3.4	0.6	0.4	0.2	0.6	0.9	1.2	(0.8)	100

	Group														
2014	AQ1 £bn	AQ2 £bn	AQ3 £bn	AQ4 £bn	AQ5 £bn	AQ6 £bn	AQ7 £bn	AQ8 £bn	AQ9 £bn	AQ10 £bn	Balances with holding company and fellow subsidiaries £bn	Past due £bn	Impaired £bn	Impairment provisions £bn	Total £bn
Cash and balances at central banks	72.6	—	1.3	0.1	—	—	—	—	—	—	—	—	—	—	74.0
Banks															
- Reverse repos	2.6	4.1	2.5	8.3	2.1	0.6	0.5	—	—	—	—	—	—	—	20.7
- Derivative cash collateral	3.7	4.6	1.2	1.4	0.2	0.1	0.1	—	—	—	—	—	—	—	11.3
- Bank loans	3.6	0.6	2.7	2.6	0.5	0.1	0.2	—	—	—	2.3	—	—	—	12.6
- Total	9.9	9.3	6.4	12.3	2.8	0.8	0.8	—	—	—	2.3	—	—	—	44.6
Customers															
- Reverse repos	27.1	0.4	8.7	5.1	1.9	—	0.8	—	—	—	—	—	—	—	44.0
- Derivative cash collateral	12.5	1.6	4.3	2.8	0.5	—	—	—	—	—	—	—	—	—	21.7
- Customer loans	26.8	16.4	22.9	103.7	58.6	34.5	22.3	5.6	4.4	0.9	1.4	6.1	25.1	(17.4)	311.3
- Total	66.4	18.4	35.9	111.6	61.0	34.5	23.1	5.6	4.4	0.9	1.4	6.1	25.1	(17.4)	377.0
Settlement balances and other financial assets	0.5	0.1	1.8	0.9	0.4	—	—	—	—	—	—	1.0	—	—	4.7
Derivatives	65.5	100.0	123.8	48.8	10.5	1.0	1.1	0.5	0.2	0.5	2.7	—	—	—	354.6
Undrawn commitments	42.6	15.7	26.4	46.3	29.2	10.3	5.5	0.6	0.3	1.1	0.1	—	—	—	178.1
Contingent liabilities	4.7	2.2	2.7	4.9	2.0	1.0	0.7	0.1	0.2	0.1	0.7	—	—	—	19.3
Total excluding disposal groups	262.2	145.7	198.3	224.9	105.9	47.6	31.2	6.8	5.1	2.6	7.2	7.1	25.1	(17.4)	1,052.3
Disposal groups - Citizens															99.7
Disposal groups - other															0.1
Total															1,152.1
Total %	25.0	13.8	18.8	21.4	10.1	4.5	3.0	0.6	0.5	0.2	0.7	0.7	2.4	(1.7)	100

Credit risk: balance sheet analysis continued

	Bank														
2015	AQ1 £bn	AQ2 £bn	AQ3 £bn	AQ4 £bn	AQ5 £bn	AQ6 £bn	AQ7 £bn	AQ8 £bn	AQ9 £bn	AQ10 £bn	Balances with holding company and fellow subsidiaries £bn	Past due £bn	Impaired £bn	Impairment provisions £bn	Total £bn
Cash and balances at central banks	74.9	—	2.0	—	—	—	—	—	—	—	—	—	—	—	76.9
Banks															
- Reverse repos	0.1	0.6	1.5	4.6	1.3	0.4	0.2	—	—	—	—	—	—	—	8.7
- Derivative cash collateral	3.4	4.6	1.4	1.2	0.2	—	—	—	—	—	—	—	—	—	10.8
- Bank loans	0.5	0.2	0.3	0.2	0.2	0.1	0.1	—	0.1	—	24.1	0.1	—	—	25.9
- Total	4.0	5.4	3.2	6.0	1.7	0.5	0.3	—	0.1	—	24.1	0.1	—	—	45.4
Customers															
- Reverse repos	15.1	—	1.3	1.2	0.5	0.1	—	—	—	—	—	—	—	—	18.2
- Derivative cash collateral	9.2	1.1	3.6	3.0	0.2	0.1	—	—	—	—	—	—	—	—	17.2
- Customer loans	10.2	5.4	8.9	35.9	18.4	7.1	6.0	1.2	0.4	0.4	28.3	2.7	2.8	(1.5)	126.2
- Total	34.5	6.5	13.8	40.1	19.1	7.3	6.0	1.2	0.4	0.4	28.3	2.7	2.8	(1.5)	161.6
Settlement balances and other financial assets	1.4	0.1	0.1	0.1	—	—	—	—	—	—	0.4	1.0	—	—	3.1
Derivatives	41.0	65.5	88.9	57.4	6.1	1.0	0.7	—	0.2	0.1	4.7	—	—	—	265.6
Undrawn commitments	14.3	5.1	17.5	25.9	13.5	2.9	2.9	0.2	0.2	0.2	5.9	—	—	—	88.6
Contingent liabilities	0.8	1.0	1.4	3.5	1.4	0.3	0.6	0.1	—	0.1	0.7	—	—	—	9.9
Total	170.9	83.6	126.9	133.0	41.8	12.0	10.5	1.5	0.9	0.8	64.1	3.8	2.8	(1.5)	651.1
Total %	26.5	12.8	19.5	20.4	6.4	1.8	1.6	0.2	0.1	0.1	9.8	0.6	0.4	(0.2)	100
2014															
Cash and balances at central banks	69.8	—	1.1	0.1	—	—	—	—	—	—	—	—	—	—	71.0
Banks															
- Reverse repos	0.4	3.9	1.6	6.0	1.8	0.6	0.5	—	—	—	—	—	—	—	14.8
- Derivative cash collateral	3.2	4.6	1.2	1.4	0.2	0.1	0.1	—	—	—	—	—	—	—	10.8
- Bank loans	1.4	0.4	0.6	1.6	0.3	—	0.2	—	—	—	24.8	—	—	—	29.3
- Total	5.0	8.9	3.4	9.0	2.3	0.7	0.8	—	—	—	24.8	—	—	—	54.9
Customers															
- Reverse repos	22.7	0.4	2.0	4.7	1.3	—	0.8	—	—	—	—	—	—	—	31.9
- Derivative cash collateral	12.5	1.6	4.3	2.8	0.5	—	—	—	—	—	—	—	—	—	21.7
- Customer loans	9.2	8.3	11.4	38.9	25.4	12.3	9.5	2.0	0.6	0.4	41.2	1.9	6.2	(3.2)	164.1
- Total	44.4	10.3	17.7	46.4	27.2	12.3	10.3	2.0	0.6	0.4	41.2	1.9	6.2	(3.2)	217.7
Settlement balances and other financial assets	0.7	0.1	0.4	0.6	0.3	—	—	—	—	—	0.5	0.8	—	—	3.4
Derivatives	65.1	99.9	123.7	48.6	10.3	0.9	0.9	0.5	0.2	0.4	9.3	—	—	—	359.8
Undrawn commitments	32.8	13.0	23.3	32.3	15.3	4.2	2.3	0.2	0.2	0.4	4.2	—	—	—	128.2
Contingent liabilities	4.6	1.9	2.3	4.0	1.4	0.6	0.5	—	0.2	—	0.7	—	—	—	16.2
Total	222.4	134.1	171.9	141.0	56.8	18.7	14.8	2.7	1.2	1.2	80.7	2.7	6.2	(3.2)	851.2
Total %	26.2	15.8	20.2	16.6	6.7	2.2	1.7	0.3	0.1	0.1	9.5	0.3	0.7	(0.4)	100

Key points

Group

- Capital Resolution's disposal strategy and other portfolio reduction strategies resulted in the non-investment grade (AQ5 and lower) portfolios decreasing by £29.3 billion (15%). Overall credit quality has remained broadly stable with about 76% (excluding cash and central bank balances) being investment grade or higher, supported by benign economic and credit conditions.
- Customer loans decreased by £22.3 billion (7%) to £289.0 billion, across most AQ bands, with investment grade loans at 59% in 2015 compared with 55% in 2014. The combined increase of £7.6 billion in AQ3 and AQ4 reflected the improved asset quality in UK PBB's book reflecting market conditions along with growth in the NW mortgage business.
- Bank loans decreased by £4.9 billion across most AQ bands.
- Reverse repos decreased by £24.9 billion, with £22.7 billion in investment grade, reflecting reduced trading activities in EMEA Rates, the wind down of US ABP business and a decrease in APAC due to the exit of trading activities in Japan, in line with balance sheet management and exit strategies.
- Derivatives decreased by £91.5 billion with reductions across all bands except AQ4 where an increase of £8.7 billion is the result of existing counterparties being downgraded due to a decrease in MTM values and new counterparties coming on at lower grades.
- Past due loans increased by £0.7 billion, primarily within CIB and Capital Resolutions.

Bank

- Capital Resolution's disposal strategy and other portfolio reduction strategies resulted in the non-investment grade (AQ5 and lower) portfolios decreasing by £27.9 billion (29%). Overall credit quality has remained broadly stable with about 76% (excluding cash and central bank balances) being investment grade or higher, supported by benign economic and credit conditions.
- Customer loans decreased by £37.9 billion (23%) to £126.2 billion, across all AQ bands, with investment grade loans at 48% in 2015 compared with 41% in 2014.
- Reverse repos decreased by £19.8 billion, with £17.3 billion in investment grade, reflecting reduced trading activities and exit strategies.
- Derivatives decreased by £94.2 billion with reductions across all bands except AQ4 where an increase of £8.8 billion is the result of existing counterparties being downgraded due to a decrease in MTM values and new counterparties coming on at lower grades.
- Past due loans increased by £1.1 billion, primarily within CIB and Capital Resolutions.

Credit risk: balance sheet analysis continued

Loans, REIL and impairment provisions

Risk elements in lending (REIL) comprises impaired loans and accruing loans past due 90 days or more as to principal or interest. Impaired loans are all loans (including loans subject to forbearance) for which an impairment provision has been established; for collectively assessed loans, impairment loss provisions are not allocated to individual loans and the entire portfolio is included in impaired loans. Accruing loans past due 90 days or more comprise loans past due 90 days where no impairment loss is expected.

Loans and related credit metrics

The tables below analyse gross loans and advances (excluding reverse repos) and the related credit metrics by reportable segment.

	Group								
					Credit metrics				
	Gross loans to								
2015	Banks £m	Customers £m	REIL £m	Provisions £m	REIL as a % of gross loans to customers %	Provisions as a % of REIL %	Provisions as a % of gross loans to customers %	Impairment losses/ (releases) £m	Amounts written-off £m
UK PBB	903	121,552	2,682	1,847	2.2	69	1.5	(6)	695
Ulster Bank RoI	1,971	18,584	3,503	1,911	18.8	55	10.3	(142)	168
Commercial Banking	665	92,002	1,911	749	2.1	39	0.8	69	263
Private Banking	54	11,230	115	37	1.0	32	0.3	13	7
RBS International	6	7,401	92	31	1.2	34	0.4	—	32
CIB	5,696	16,076	—	1	—	nm	—	(7)	—
Capital Resolution	5,949	24,484	3,271	2,200	13.4	67	9.0	(775)	7,675
W&G	—	20,291	461	275	2.3	60	1.4	15	110
Central items & other	1,944	418	—	1	—	—	0.2	(1)	—
Total third party	17,188	312,038	12,035	7,052	3.9	59	2.3	(834)	8,950
Amounts due from holding company and fellow subsidiaries	1,557	1,258	—	—	—	—	—	—	—
Disposal groups	642	1,659	20	20	1.2	100	1.2	—	—
Total	19,387	314,955	12,055	7,072	3.8	59	2.2	(834)	8,950
2014									
UK PBB	866	114,202	3,571	2,557	3.1	72	2.2	154	673
Ulster Bank RoI	1,037	20,522	4,366	2,383	21.3	55	11.6	(306)	91
Commercial Banking	797	85,719	2,483	919	2.9	37	1.1	85	376
Private Banking	53	10,984	126	31	1.1	25	0.3	(5)	26
RBS International	9	7,261	103	62	1.4	60	0.9	(7)	72
CIB	2,548	26,518	—	16	—	nm	0.1	(7)	—
Capital Resolution	13,379	60,774	15,435	11,041	25.4	72	18.2	(1,282)	3,565
W&G	—	19,843	616	374	3.1	61	1.9	55	95
Central items & other	2,902	3,169	22	21	0.7	95	0.7	(13)	55
Total third party	21,591	348,992	26,722	17,404	7.7	65	5.0	(1,326)	4,953
Amounts due from holding company and fellow subsidiaries	2,333	1,323	—	—	—	—	—	—	—
Disposal groups	1,745	60,142	1,330	536	2.2	40	0.9	194	300
Total	25,669	410,457	28,052	17,940	6.8	64	4.4	(1,132)	5,253

Key points

- Loans to banks decreased by £4.4 billion primarily in Capital Resolution due to wind-downs in the EMEA and APAC regions (£1.7 billion) as well as lower derivative collateral requirements. Ulster Banks RoI's increased bank loans reflected higher cash deposits with central banks.
- Customer loans declined by £37.0 billion or 11% to £312.0 billion reflecting the run-down strategy being partially offset by core loan book.
- UK PBB: mortgage growth of £9.3 billion was the principal driver of the £7.4 billion gross lending increase in 2015 and £13.1 billion increase in the last two years reflecting strategy and investment. Unsecured balances continued to decline gradually, albeit at a much slower rate.
- Commercial Banking: of the £6.3 billion loan increase, £5.0 billion related to UK and Western Europe loans transferred from CIB and £1.4 billion loan growth that despite £2.2 billion of strategic write-off and disposals.
- Ulster Bank RoI: Lending decreased by £1.9 billion. Strong new lending volumes were offset by high levels of customer repayments, the sale of a £0.3 billion buy-to-let mortgage portfolio and exchange rate movements. Tracker mortgages portfolio reduced by £1.4 billion to £9.2 billion, making up two thirds of the mortgage book, and commercial real estate lending fell by £0.4 billion.
- CIB: lending fell by £10.4 billion, £5.0 billion reflecting the transfers to Commercial Banking and the rest primarily derivative collateral reduction.
- Capital Resolution lending fell by £36.3 billion and included loan sales in US £3.1 billion, APAC £2.2 billion and EMEA £0.5 billion (relating to sale of Russian portfolio). Reductions in GTS and Shipping of £6.8 billion following customer wind-downs as well as £10.6 billion of maturities and repayments across the loan portfolio in all regions also contributed to the significant reduction.
- Risk elements in lending (REIL) declined by £14.7 billion to £12.0 billion, with REIL as a percentage of gross loans falling from 7.7% to 3.9%. The reduction was primarily driven by the disposals in RCR within Capital Resolution.
- Net impairment releases of £834 million were 37% lower compared with net impairment releases of £1,326 million in 2014. Although releases were at lower levels than in 2014, credit quality remained stable with continued increased recoveries in certain businesses.
- Capital Resolution recorded net releases of £775 million, compared with £1,282 million, with disposal activity continuing. Ulster Bank RoI recorded net impairment releases of £142 million, a reduction from £306 million, as economic conditions in Ireland continue to improve whilst UK PBB recorded a release of £6 million compared with a loss of £154 million, due to lower debt flows and increased releases and recoveries. Net releases were reported also in CIB, although at more modest levels.
- Amounts written-off increased by £4.0 billion of which £6.2 billion related to commercial real estate.
- Loan impairment provisions were 41% of the level at 2014 year end at £7.1 billion and covered REIL by 59% compared with 65% last year reflecting economic and credit conditions.
- Provisions were 2.3% of gross loans, significantly lower than 5.0% last year.
- Refer to Credit risk - Key credit portfolios for key sector concentrations and Problem debt management section for risk management approaches.

Credit risk: balance sheet analysis continued

Sector and geographical concentration

The tables below analyse gross loans and advances to banks and customers (excluding reverse repos) and related credit metrics by sector and geography based on the location of lending office. Ulster Bank RoI contributes a significant proportion of the European loan exposure. Refer to Business review on page 10.

	Group							
				Credit metrics				
2015	Gross loans £m	REIL £m	Provisions £m	REIL as a % of gross loans %	Provisions as a % of REIL %	Provisions as a % of gross loans %	Impairment losses/(releases) £m	Amounts written-off £m
Central and local government	6,670	1	1	—	100	—	—	—
Finance	31,375	76	57	0.2	75	0.2	(5)	165
Personal - mortgages (1)	137,465	3,634	1,002	2.6	28	0.7	(82)	171
- unsecured	15,120	1,311	1,131	8.7	86	7.5	122	513
Property	35,720	3,482	1,990	9.7	57	5.6	(555)	5,999
Construction	4,411	357	269	8.1	75	6.1	(14)	313
of which: Commercial real estate	*27,454*	*3,560*	*2,054*	*13.0*	*58*	*7.5*	*(807)*	*6,151*
Manufacturing	9,645	255	148	2.6	58	1.5	3	140
Finance leases and instalment credit	11,435	107	79	0.9	74	0.7	(8)	37
Retail, wholesale and repairs	12,000	422	292	3.5	69	2.4	7	325
Transport and storage	8,804	559	254	6.3	45	2.9	114	370
Health, education and leisure	10,959	394	190	3.6	48	1.7	15	171
Hotels and restaurants	5,363	336	201	6.3	60	3.7	1	346
Utilities	3,392	91	46	2.7	51	1.4	11	27
Other	19,679	1,010	810	5.1	80	4.1	(37)	340
Latent	—	—	582	—	—	—	(402)	—
Total third-party	312,038	12,035	7,052	3.9	59	2.3	(830)	8,917
Amounts due from holding company and fellow subsidiaries	1,258	—	—	—	—	—	—	—
Disposal groups	1,659	20	20	1.2	100	1.2	—	—
Total customers	314,955	12,055	7,072	3.8	59	2.2	(830)	8,917
Of which:								
UK								
Personal - mortgages (1)	123,653	1,083	158	0.9	15	0.1	17	36
- unsecured	14,348	1,262	1,085	8.8	86	7.6	126	501
Property and construction	38,005	2,814	1,282	7.4	46	3.4	28	2,773
of which: Commercial real estate	*25,676*	*2,568*	*1,107*	*10.0*	*43*	*4.3*	*(118)*	*2,575*
Other	109,717	2,194	1,180	2.0	54	1.1	125	800
Latent	—	—	330	—	—	—	(300)	—
	285,723	7,353	4,035	2.6	55	1.4	(4)	4,110
Europe								
Personal - mortgages (1)	13,776	2,550	844	18.5	33	6.1	(101)	135
- unsecured	772	49	45	6.3	92	5.8	(5)	12
Property and construction	1,993	1,008	966	50.6	96	48.5	(593)	3,539
of which: Commercial real estate	*1,628*	*974*	*935*	*59.8*	*96*	*57.4*	*(688)*	*3,576*
Other	6,914	949	836	13.7	88	12.1	—	1,014
Latent	—	—	252	—	—	—	(102)	—
	23,455	4,556	2,943	19.4	65	12.5	(801)	4,700
Banks	17,188	1	1	—	100	—	(4)	33
Amounts due from holding company and fellow subsidiaries	1,557	—	—	—	—	—	—	—
Disposal groups	642	—	—	—	—	—	—	—
Total banks	19,387	1	1	—	100	—	(4)	33

Note:
(1) Mortgages are reported in sectors other than personal mortgages by certain businesses based on the nature of the relationship with the customer.

2014	Gross loans £m	REIL £m	Provisions £m	Group Credit metrics: REIL as a % of gross loans %	Provisions as a % of REIL %	Provisions as a % of gross loans %	Impairment losses/(releases) £m	Amounts written-off £m
Central and local government	8,472	1	1	—	100	—	(1)	—
Finance	37,660	333	227	0.9	68	0.6	2	23
Personal - mortgages (1)	129,671	4,682	1,372	3.6	29	1.1	(16)	89
- unsecured	17,980	1,769	1,536	9.8	87	8.5	299	608
Property	46,507	12,939	8,882	27.8	69	19.1	(1,084)	2,608
Construction	5,287	970	611	18.3	63	11.6	75	199
of which: Commercial real estate	*43,317*	*13,291*	*9,014*	*30.7*	*68*	*20.8*	*(1,067)*	*2,745*
Manufacturing	15,696	416	298	2.7	72	1.9	(21)	176
Finance leases and instalment credit	11,265	156	113	1.4	72	1.0	—	75
Retail, wholesale and repairs	15,582	936	637	6.0	68	4.1	109	155
Transport and storage	13,120	1,130	496	8.6	44	3.8	34	211
Health, education and leisure	12,392	704	358	5.7	51	2.9	1	344
Hotels and restaurants	6,084	1,089	574	17.9	53	9.4	(36)	109
Utilities	4,516	105	64	2.3	61	1.4	28	3
Other	24,760	1,450	1,188	5.9	82	4.8	(19)	344
Latent	—	—	1,007	—	—	—	(687)	—
Total third-party	348,992	26,680	17,364	7.6	65	5.0	(1,316)	4,944
Amounts due from holding company and fellow subsidiaries	1,323	—	—	—	—	—	—	—
Disposal groups	60,142	1,330	536	2.2	40	0.9	194	300
Total customers	410,457	28,010	17,900	6.8	64	4.4	(1,122)	5,244
Of which:								
UK								
Personal - mortgages (1)	113,520	1,394	191	1.2	14	0.2	(23)	76
- unsecured	15,923	1,674	1,452	10.5	87	9.1	290	546
Property and construction	41,634	6,694	4,036	16.1	60	9.7	(222)	2,081
of which: Commercial real estate	*29,359*	*6,361*	*3,799*	*21.7*	*60*	*12.9*	*(181)*	*2,024*
Other	113,024	3,283	1,823	2.9	56	1.6	91	848
Latent	—	—	635	—	—	—	(231)	—
	284,101	13,045	8,137	4.6	62	2.9	(95)	3,551
Europe								
Personal - mortgages (1)	15,629	3,268	1,178	20.9	36	7.5	7	9
- unsecured	1,046	76	66	7.3	87	6.3	9	66
Property and construction	9,076	7,196	5,442	79.3	76	60.0	(784)	723
of which: Commercial real estate	*7,874*	*6,901*	*5,200*	*87.6*	*75*	*66.0*	*(886)*	*702*
Other	18,861	2,759	1,949	14.6	71	10.3	30	559
Latent	—	—	372	—	—	—	(456)	—
	44,612	13,299	9,007	29.8	68	20.2	(1,194)	1,357
Banks	21,591	42	40	0.2	95	0.2	(10)	9
Amounts due from holding company and fellow subsidiaries	2,333	—	—	—	—	—	—	—
Disposal groups	1,745	—	—	—	—	—	—	—
Total banks	25,669	42	40	0.2	95	0.2	(10)	9

Note:
(1) Mortgages are reported in sectors other than personal mortgages by certain businesses based on the nature of the relationship with the customer.

Credit risk: balance sheet analysis continued

REIL and impairments flow statements

2015	REIL excluding Citizens (1) £m	Citizens REIL (1) £m	Total REIL (1) £m	Impairment provisions excluding Citizens £m	Citizens impairment provisions £m	Total impairment provisions £m
At beginning of year	26,722	1,330	28,052	17,404	536	17,940
Currency translation and other adjustments	(865)	29	(836)	(576)	17	(559)
Additions	4,075	174	4,249	—	—	—
Transfers between REIL and potential problem loans	(222)	—	(222)	—	—	—
Transfer to performing book	(1,120)	—	(1,120)	—	—	—
Repayments and disposals	(7,585)	(1,353)	(8,938)	—	(554)	(554)
Amounts written-off	(8,950)	(180)	(9,130)	(8,950)	(180)	(9,130)
Recoveries of amounts previously written-off	—	—	—	172	78	250
Release to the income statement from continuing operations	—	—	—	(834)	—	(834)
Charge to the income statement from discontinued operations	—	—	—	—	103	103
Unwind of discount	—	—	—	(144)	—	(144)
At end of year	12,055	—	12,055	7,072	—	7,072
2014						
At beginning of year	37,803	1,323	39,126	24,536	518	25,054
Currency translation and other adjustments	(1,115)	75	(1,040)	(704)	21	(683)
Additions	6,594	335	6,929	—	—	—
Transfers between REIL and potential problem loans	(257)	—	(257)	—	—	—
Transfer to performing book	(1,460)	—	(1,460)	—	—	—
Repayments and disposals	(9,890)	(103)	(9,993)	—	—	—
Amounts written-off	(4,953)	(300)	(5,253)	(4,953)	(300)	(5,253)
Recoveries of amounts previously written-off	—	—	—	98	103	201
Release to the income statement from continuing operations	—	—	—	(1,326)	—	(1,326)
Charge to the income statement from discontinued operations	—	—	—	—	194	194
Unwind of discount	—	—	—	(247)	—	(247)
At end of year	26,722	1,330	28,052	17,404	536	17,940

REIL elements in lending

The table below analyses REIL between UK and overseas, based on the location of the lending office.

	2015		2014					
			Impaired loans			Accruing past due		
	REIL Impaired loans £m	REIL Accruing past due £m	REIL excluding Citizens (1) £m	Citizens REIL (1) £m	Total REIL (1) £m	REIL excluding Citizens (1) £m	Citizens REIL (1) £m	Total REIL (1) £m
- UK	6,091	1,262	11,550	—	11,550	1,535	—	1,535
- overseas	4,677	25	13,532	1,330	14,862	105	—	105
Total REIL	10,768	1,287	25,082	1,330	26,412	1,640	—	1,640

Notes:
(1) REIL are stated without giving effect to any security held that could reduce the eventual loss should it occur or to any provisions marked.
(2) For details on impairment methodology refer to Credit risk on page 70 and Accounting policy 15 Impairment of financial assets on page 154.

Past due analysis

The table below shows loans and advances to customers that were past due at the balance sheet date but are not considered impaired.

	2015 £m	2014 £m
Past due 1-29 days	4,150	3,050
Past due 30-59 days	769	784
Past due 60-89 days	530	586
Past due 90 days or more	1,287	1,640
Total excluding Citizens	6,736	6,060
Citizens	—	2,112
Total	6,736	8,172

Past due analysis by sector

Personal	3,437	3,554
Property and construction	1,341	1,183
Financial institution	187	60
Other corporate	1,771	1,263
Total excluding Citizens	6,736	6,060
Citizens	—	2,112
Total	6,736	8,172

Credit risk: balance sheet analysis continued

Securities and AFS reserves

Debt securities

The table below analyses debt securities by issuer and IFRS measurement classifications and includes disposal groups. US central and local government includes US federal agencies. The other financial institutions category includes US government sponsored agencies and securitisation entities, the latter principally relating to asset-backed securities (ABS). Ratings are based on the lowest of Standard & Poor's, Moody's and Fitch.

	Central and local government				Other financial			Of which
2015	UK £m	US £m	Other £m	Banks £m	institutions £m	Corporate £m	Total £m	ABS £m
Held-for-trading (HFT)	4,107	4,627	22,222	576	3,591	636	35,759	707
Available-for-sale	9,110	10,265	11,293	1,639	4,670	15	36,992	2,252
Loans and receivables	—	—	—	—	2,221	144	2,365	2,222
Held-to-maturity	4,911	—	—	—	—	—	4,911	—
Long positions excluding disposal groups	18,128	14,892	33,515	2,215	10,482	795	80,027	5,181
Disposal groups	14	94	122	162	21	6	419	139
Total including disposal groups	18,142	14,986	33,637	2,377	10,503	801	80,446	5,320
Of which US agencies	—	—	—	—	806	—	806	—
Short positions (HFT)	(4,697)	(3,347)	(11,796)	(391)	(410)	(165)	(20,806)	—
Available-for-sale								
AFS reserves (gross of tax)	12	(78)	88	5	152	4	183	73
Gross unrealised gains - excluding disposal groups	383	104	267	3	105	7	869	88
Gross unrealised gains - disposal groups	—	—	1	3	—	—	4	2
Gross unrealised gains - total	383	104	268	6	105	7	873	90
Gross unrealised losses - excluding disposal groups	(7)	(62)	(9)	(1)	(33)	(3)	(115)	(16)
Gross unrealised losses - total	(7)	(62)	(9)	(1)	(33)	(3)	(115)	(16)
Of which:								
less than 12 months	(7)	(58)	(9)	(1)	(17)	(3)	(95)	—
more than 12 months	—	(4)	—	—	(16)	—	(20)	(16)
2014								
Held-for-trading	6,218	7,709	24,448	1,385	7,366	1,976	49,102	3,559
Designated as at fair value	—	—	—	—	1	—	1	—
Available-for-sale	4,747	5,230	9,472	3,276	4,769	46	27,540	3,488
Loans and receivables	—	—	—	179	2,751	138	3,068	2,714
Held-to-maturity	4,537	—	—	—	—	—	4,537	—
Long positions excluding Citizens	15,502	12,939	33,920	4,840	14,887	2,160	84,248	9,761
Citizens	—	5,781	—	—	9,512	—	15,293	15,275
Issued by RBS Group companies	—	—	—	6	17	3	26	—
Total	15,502	18,720	33,920	4,846	24,416	2,163	99,567	25,036
Of which US agencies	—	6,222	—	—	10,860	—	17,082	16,053
Short positions (HFT)	(4,167)	(6,413)	(10,276)	(557)	(673)	(730)	(22,816)	—
Available-for-sale								
AFS reserves (gross of tax)	54	(52)	77	8	318	5	410	178
Gross unrealised gains - excluding Citizens	451	144	300	8	142	6	1,051	128
Gross unrealised gains - Citizens	—	66	—	—	195	—	261	261
Gross unrealised gains - total	451	210	300	8	337	6	1,312	389
Gross unrealised losses - excluding Citizens	(1)	(5)	(1)	—	(56)	(2)	(65)	(56)
Gross unrealised losses - Citizens	—	(112)	—	—	(25)	—	(137)	(137)
Gross unrealised losses - total	(1)	(117)	(1)	—	(81)	(2)	(202)	(193)
Of which:								
less than 12 months	(1)	(82)	(1)	—	(5)	—	(89)	(85)
more than 12 months	—	(35)	—	—	(76)	(2)	(113)	(108)

Key points

- Total debt securities decreased by £4.2 billion (5%) during 2015, driven by lower held-for-trading positions across all issuer types, largely offset by an increase in available-for-sale securities in Treasury's liquidity portfolio.
- HFT: Decreases were due to exit of trading businesses, novation of equities portfolio, balance sheet reduction and risks.
- AFS: Increases were due to build up of AFS securities within the liquidity portfolio by Treasury for the Group. Assets underlying the Group's ABS portfolio were more than 80% of European origin compared with 65% a year ago on a like for like basis reflecting the exit from the US asset-backed product business as well as other reductions in Capital Resolution.

Credit risk: balance sheet analysis continued

Ratings

The table below analyses debt securities by issuer and external ratings. Ratings are based on the lowest of Standard and Poor's, Moody's and Fitch.

	Group							
	Central and local government				Other financial			Of which
2015	UK £m	US £m	Other £m	Banks £m	institutions £m	Corporate £m	Total £m	ABS £m
AAA	—	—	11,603	1,551	5,217	3	18,374	3,227
AA to AA+	18,128	14,892	6,860	102	1,424	60	41,466	261
A to AA-	—	—	8,737	420	1,881	147	11,185	335
BBB- to A-	—	—	5,973	79	845	214	7,111	363
Non-investment grade	—	—	342	32	526	200	1,100	446
Unrated	—	—	—	31	589	171	791	549
Total excluding disposal groups	18,128	14,892	33,515	2,215	10,482	795	80,027	5,181
Disposal groups	14	94	122	162	21	6	419	139
Total	18,142	14,986	33,637	2,377	10,503	801	80,446	5,320
2014								
AAA	—	—	15,495	1,319	5,138	64	22,016	3,816
AA to AA+	15,502	12,939	9,520	282	4,009	118	42,370	3,056
A to AA-	—	—	4,413	2,542	2,413	340	9,708	567
BBB- to A-	—	—	4,120	277	1,176	669	6,242	845
Non-investment grade	—	—	275	50	713	603	1,641	640
Unrated	—	—	97	370	1,438	366	2,271	837
Total excluding Citizens	15,502	12,939	33,920	4,840	14,887	2,160	84,248	9,761
Citizens	—	5,781	—	—	9,512	—	15,293	15,275
Issued by holding company and fellow subsidiaries	—	—	—	6	17	3	26	—
Total	15,502	18,720	33,920	4,846	24,416	2,163	99,567	25,036

	Bank							
	Central and local government				Other financial			Of which
2015	UK £m	US £m	Other £m	Banks £m	institutions £m	Corporate £m	Total £m	ABS £m
AAA	—	—	10,964	1,540	4,850	3	17,357	3,227
AA to AA+	18,128	10,863	5,976	51	621	55	35,694	258
A to AA-	—	—	8,736	153	1,881	136	10,906	335
BBB- to A-	—	—	5,973	73	820	198	7,064	363
Non-investment grade	—	—	342	32	524	200	1,098	446
Unrated	—	—	—	31	588	156	775	549
	18,128	10,863	31,991	1,880	9,284	748	72,894	5,178
Issued by holding company and fellow subsidiaries	—	—	—	—	3,708	—	3,708	3,069
	18,128	10,863	31,991	1,880	12,992	748	76,602	8,247
2014								
AAA	—	—	13,667	1,075	4,985	65	19,792	3,655
AA to AA+	15,382	6,353	9,170	244	1,237	107	32,493	980
A to AA-	—	—	4,300	2,025	2,376	307	9,008	544
BBB- to A-	—	—	4,078	261	1,129	311	5,779	838
Non-investment grade	—	—	275	43	699	593	1,610	634
Unrated	—	—	97	370	1,401	348	2,216	800
	15,382	6,353	31,587	4,018	11,827	1,731	70,898	7,451
Issued by holding company and fellow subsidiaries	—	—	—	—	16,696	—	16,696	16,049
	15,382	6,353	31,587	4,018	28,523	1,731	87,594	23,500

Asset-backed securities

The table below summarises the ratings of asset-backed securities on the balance sheet.

2015	RMBS (1) Government sponsored or similar (2) £m	RMBS (1) Prime £m	RMBS (1) Non-conforming £m	RMBS (1) Sub-prime £m	CMBS (1) £m	CDOs & CLOs £m	Other ABS £m	Total £m
AAA	—	266	749	2	—	77	2,133	3,227
AA to AA+	—	2	150	—	1	12	96	261
A to AA-	—	4	24	5	13	9	280	335
BBB- to A-	—	13	144	20	21	121	44	363
Non-investment grade (3)	—	23	25	143	24	169	62	446
Unrated (3)	—	10	—	1	470	25	43	549
Total excluding disposal groups	—	318	1,092	171	529	413	2,658	5,181
Disposal groups	—	—	—	—	—	—	139	139
Total	—	318	1,092	171	529	413	2,797	5,320
2014								
AAA	—	1,471	775	14	30	33	1,493	3,816
AA to AA+	2,012	2	657	17	151	78	139	3,056
A to AA-	—	82	27	3	41	17	397	567
BBB- to A-	—	84	137	12	18	63	531	845
Non-investment grade (3)	—	14	38	135	65	292	96	640
Unrated (3)	—	22	—	24	474	40	277	837
Total excluding Citizens	2,012	1,675	1,634	205	779	523	2,933	9,761
Citizens	10,894	1,155	223	—	3,003	—	—	15,275
Total	12,906	2,830	1,857	205	3,782	523	2,933	25,036

Notes:
(1) Residential mortgage-backed securities; Commercial mortgage-backed securities.
(2) Includes US agency.
(3) Includes held-for-trading.

Credit risk: balance sheet analysis continued

Equity shares

The table below analyses holdings of equity shares for eurozone countries and other countries with balances of more than £50 million by country, issuer and measurement classification. The HFT are used mainly for economic hedging of debt issuances and equity derivatives. The AFS balances are individually small holdings in unlisted companies, mainly acquired through debt for equity transactions in Restructuring.

	2015										
	HFT					AFS/DFV (1)					
Countries	Banks £m	Other financial institutions (2) £m	Corporate £m	Total £m	HFT short positions £m	Banks £m	Other financial institutions (2) £m	Corporate £m	Total AFS/DFV £m	Total £m	AFS reserves £m
Luxembourg	—	98	—	98	—	—	—	—	—	98	—
Other	1	35	28	64	(2)	5	5	5	15	79	—
Total eurozone	1	133	28	162	(2)	5	5	5	15	177	—
US	—	23	7	30	—	—	40	2	42	72	3
UK	—	50	174	224	—	—	371	12	383	607	230
Japan	—	—	70	70	—	—	1	—	1	71	—
Australia	22	22	19	63	—	—	—	—	—	63	—
Other	12	8	32	52	—	—	26	1	27	79	42
Total excluding disposal groups	35	236	330	601	(2)	5	443	20	468	1,069	275
Disposals groups	—	—	—	—	—	—	24	—	24	24	20
Total	35	236	330	601	(2)	5	467	20	492	1,093	295
2014											
Total excluding Citizens	367	972	3,385	4,724	(212)	5	281	193	479	5,203	99
Citizens	—	—	—	—	—	305	263	4	572	572	(2)
Total	367	972	3,385	4,724	(212)	310	544	197	1,051	5,775	97

Notes:
(1) Designated as at fair value through profit or loss balances are £71 million (2014 - £239 million), of which £61 million are other financial institutions (2014 - £69 million) and £10 million are corporate (2014 - £170 million).
(2) Includes government sponsored entities.

Derivatives

Summary

The table below analyses the fair value of the Group's derivatives by type of contract. Master netting arrangements in respect of mark-to-market (mtm) positions and collateral shown below do not result in a net presentation in the Group's balance sheet under IFRS.

	2015			2014		
	Notional £bn	Assets £m	Liabilities £m	Notional £bn	Assets £m	Liabilities £m
Interest rate	19,766	205,564	194,740	27,288	268,114	259,440
Exchange rate	3,697	54,789	57,946	4,640	78,373	83,217
Credit	66	908	839	124	2,238	2,605
Equity and commodity	18	547	740	78	3,119	3,516
	23,547	261,808	254,265	32,130	351,844	348,778
Counterparty mark-to-market netting		(214,790)	(214,790)		(295,177)	(295,177)
Cash collateral		(27,614)	(25,729)		(32,629)	(30,016)
Securities collateral		(7,535)	(8,213)		(7,005)	(14,433)
Net exposure before Citizens and other disposal groups		11,869	5,533		17,033	9,152
Citizens		n/a	n/a		402	144
Other disposal groups	2	30	28	—	—	—
Total net exposure		11,899	5,561		17,435	9,296
Balances with Group companies	34	1,275	1,283	43	2,738	2,005

Credit risk: balance sheet analysis continued

Valuation reserves

When valuing financial instruments in the trading book, adjustments are made to mid-market valuations to cover bid-offer spread, liquidity and credit risk. The following table shows credit valuation adjustments (CVA) and other valuation reserves. CVA represents an estimate of the adjustment to fair value that a market participant would make to incorporate the risk inherent in derivative exposures. For discussion of CVA methodology, refer to Financial instruments - valuation on page 186.

	2015 £m	2014 £m
Credit valuation adjustments	752	1,372
Other valuation reserves		
- bid-offer	304	395
- funding valuation adjustment	745	708
- product and deal specific	619	613
	1,668	1,716
Valuation reserves	2,420	3,088

Key points

- CVA decreased over the period, driven by market movements, principally interest rates, reducing net uncollateralised derivative exposures, realised default losses and tear-ups during 2015.
- Bid-offer reserve decreases were largely driven by risk reduction in CIB.
- Other reserves were broadly unchanged, although FVA increased as a result of market movements during 2015.

Credit derivatives

The Group trades credit derivatives to meet client needs and to mitigate its own credit risk. Credit derivative exposures relating to proprietary trading are minimal. The table below analyses bought and sold protection.

	2015				2014			
	Notional		Fair value		Notional		Fair value	
Group	Bought £bn	Sold £bn	Bought £bn	Sold £bn	Bought £bn	Sold £bn	Bought £bn	Sold £bn
Client-led trading/residual risk (1)	21.9	16.5	—	0.2	52.0	49.9	0.9	1.4
Credit hedging - banking book (2)	0.9	—	0.1	—	1.8	—	0.1	—
Credit hedging - trading book								
- rates	15.1	9.4	(0.2)	(0.1)	13.8	5.8	0.2	0.3
- credit and mortgage markets	1.3	0.7	0.2	0.1	0.4	—	0.2	—
- other	0.4	—	—	—	0.4	—	—	—
	39.6	26.6	0.1	0.2	68.4	55.7	1.4	1.7

	2015		2014	
Of which:	Notional £bn	Net exposure £bn	Notional £bn	Net exposure £bn
Monoline insurers	0.5	0.1	0.1	—
CDPCs	8.4	—	15.2	—

Notes:
(1) Residual risk relates to legacy positions in Capital Resolution in 2014.
(2) Credit hedging in the banking book principally relates to portfolio management in Capital Resolution.

Market risk

Definition

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

The Group is exposed to traded market risk through its trading activities and to non-traded market risk as a result of its banking activities. In many respects, it manages its traded and non-traded market risk exposures separately, largely in line with the regulatory definitions of the trading and non-trading books.

The Group is exposed to traded market risk through its trading activities and to non-traded market risk as a result of its banking activities. In many respects, it manages its traded and non-traded market risk exposures separately, largely in line with the regulatory definitions of the trading and non-trading books.

The following disclosures in this section are audited:

- Traded market risk - Internal VaR
- Non-traded market risk - Interest rate risk VaR; internal VaR for non-trading book (primarily CIB and Capital Resolution); Structured credit portfolio; Foreign exchange risk

Disclosures in this section relate either to the Group as a whole or to individual legal entities on a solo basis within the Group. The choice reflects either the way the Group manages the risk or the basis on which it reports the risk measure to the regulator.

The following disclosures are presented on an individual legal entity basis:

- Traded market risk:
  - Internal VaR
  - Regulatory VaR back-testing
  - Minimum capital requirements
- Non-traded market risk:
  - Internal VaR for non-trading book (primarily CIB and Capital Resolution)

The legal entities have been selected based on their materiality for the risk measure in question.

All other disclosures are on an overall Group basis.

The introductory sentence to each table or graph indicates the basis of presentation of the disclosure.

Key developments in 2015*

During 2015, the Group continued to align its business with strategy, with an impact on both traded and non-traded market risk. Overall, this resulted in a further reduction of risk, a notable driver of which was the exit from a significant part of US asset-backed product (ABP) trading in the first half of the year.

Following the restructuring of the CIB business in Q4 2015, the Market Risk function adjusted to the new structure and re-calibrated its market risk limits.

Value-at-risk (VaR) remained volatile, reflecting a number of geopolitical developments and macroeconomic factors, as detailed on page 121.

*unaudited

The increased market volatility and reduced liquidity were also the key drivers of the back-testing exceptions recorded by the VaR models of RBS plc and NatWest Plc. For more information, refer to page 121.

The completion of the disposal of Citizens during the year further reduced the non-traded market risk exposures arising mainly from its retail and commercial banking activities and Treasury portfolios.

Sources of risk*

Traded market risk

The majority of traded market risk exposure arises in CIB and Capital Resolution.

The primary objective of the Group's trading activities is to provide a range of financing, risk management and investment services to its customers - including major corporations and financial institutions around the world. From a market risk perspective, the trading activities are included within the following markets: currencies; emerging markets; rates; asset-backed products; and traded credit.

The Group undertakes transactions in financial instruments including debt securities, loans, deposits and equities, as well as securities financing and derivatives.

Some of these transactions involve trading or clearing financial instruments on an exchange, including interest rate swaps, futures and options. Holders of these instruments provide margin on a daily basis with cash or other security at the exchange.

Other products are not transacted on an exchange. Of these over-the-counter transactions, those with standard terms may be cleared through central counterparties, while those that are more complex are settled directly with the counterparty and may give rise to counterparty credit risk. For more information on the management of counterparty credit risk, refer to the Credit risk section on page 70.

Non-traded market risk

The majority of non-traded market risk exposure arises from retail and commercial banking activities in all franchises from assets and liabilities that are not classified as held for trading.

Non-traded market risk is largely managed in line with the following three key categories: interest rate risk; foreign exchange risk; and equity risk.

Interest rate risk

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

NTIRR comprises four primary risk factors: repricing risk, yield curve risk, basis risk and optionality risk. For more information, refer to page 130.

Market risk continued

Foreign exchange risk

Non-traded foreign exchange risk exposures arise from two main sources:

- Structural foreign exchange risk - arising from the capital deployed in foreign subsidiaries, branches and joint arrangements and related currency funding where it differs from sterling; and
- Transactional foreign exchange risk - arising from customer transactions and profits and losses that are in a currency other than the functional currency of the transacting operation.

Equity risk

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

Pension risk

Pension-related activities also give rise to market risk. Refer to pages 64 to 66 for more information on risk related to pensions.

Risk governance*

The RBS Group's Market Risk function is responsible for identifying, measuring, monitoring and controlling the market risk arising from both trading and non-trading activities.

For general information on risk governance, refer to the Risk governance section on page 30.

More specific information on the governance, management and measurement of traded and non-traded market risk is provided in each of the dedicated sections below.

Risk appetite*

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

Its quantitative market risk appetite is expressed in terms of limits for the trading and non-trading activities that are consistent with business plans.

The Director of Market Risk cascades the limits further down the organisation as required. For each trading business, a document known as a dealing authority compiles details of all applicable limits and trading restrictions.

The limit framework at RBS Group level comprises VaR, stressed value-at-risk (SVaR) and sensitivity and stress limits (for more details on VaR and SVaR, refer to pages 121 to 126). The limit framework at trading unit level also comprises additional metrics that are specific to the market risk exposures within its scope. These additional metrics aim to control various risk dimensions such as product type, exposure size, aged inventory, currency and tenor.

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

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

For further information on risk appetite, refer to page 35.

Risk controls and assurance

For information on risk controls and assurance, refer to page 33.

Traded market risk

Risk assessment

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

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

Risk monitoring*

Traded market risk exposures are monitored against limits and analysed daily by market risk reporting and control functions. A daily report that summarises market risk exposures against the limits set by the Executive Risk Forum is sent to the RBS Group Chief Risk Officer and market risk managers across the function.

The market risk function also prepares daily risk reports that detail exposures against a more granular set of limits and triggers.

Limit reporting is supplemented with regulatory capital and stress testing information as well as ad hoc reporting.

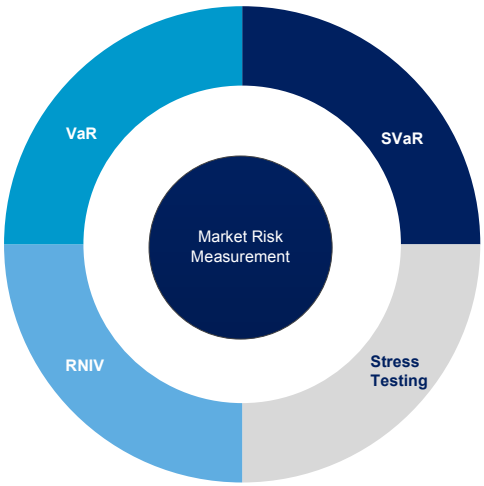
A market risk update is also included in the RBS Group Risk Management Monthly Report provided to the Executive Committee, the Board Risk Committee and the RBS Group Board. The update focuses on risk profiles relative to risk appetite; it also covers the key risks and trends, together with a discussion of relevant issues and market topics.

The reporting and updates facilitate frequent reviews and discussions of traded market risk exposures and related issues between the market risk function, senior management and the front office.

*unaudited

Risk measurement

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



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

The key inputs into these measurement methods are market data and sensitivities. Sensitivities refer to the changes in deal or portfolio value that result from small changes in market parameters that are subject to the market risk limit framework.

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

Value-at-risk*

VaR is a statistical estimate of the potential change in the market value of a portfolio (and, thus, the impact on the income statement) over a specified time horizon at a given confidence level.

For internal risk management purposes, VaR assumes a time horizon of one trading day and a confidence level of 99%. The VaR model is based on a historical simulation, utilising market data from the previous 500 days on an equally weighted basis.

The Group's internal traded VaR model captures all trading book positions including those products approved by the regulator. For an explanation of the distinction between internal VaR and regulatory VaR, refer to page 126.

The internal VaR model captures the potential impact on the income statement of the following risk factors:

- Interest rate risk - which arises from the impact of changes in interest rates and volatilities on cash instruments and derivatives. This includes interest rate tenor basis risk and cross-currency basis risk.
- Credit spread risk - which arises from the impact of changes in the credit spreads of sovereign bonds, corporate bonds, securitised products and credit derivatives.
- Currency risk - which arises from the impact of changes in currency rates and volatilities.
- Equity risk - which arises from the impact of changes in equity prices, volatilities and dividend yields.
- Commodity risk - which arises from the impact of changes in commodity prices and volatilities.

The following types of risk - which are components of the above-mentioned factors - are also considered:

- Basis risk - which is the risk that imperfect correlation between two instruments in a hedging strategy creates the potential for excess gains or losses, thus adding risk to the position;
- Prepayment risk - which is the risk associated with early unscheduled return of principal on a fixed rate security; and
- Inflation risk - which is the risk of a decrease in the value of instruments as a result of changes in inflation rates and associated volatilities.

VaR limitations*

Historical VaR and the Group's implementation of this risk measurement methodology have a number of known limitations, as summarised below, and VaR should be interpreted in light of these. The approach taken is to supplement VaR with other risk metrics that address these limitations to ensure appropriate coverage of all material market risks.

Historical simulation VaR may not provide the best estimate of future market movements. It can only provide a forecast of portfolio losses based on events that occurred in the past. The Group model uses the previous 500 days of data; this period represents a balance between model responsiveness to recent shocks and risk factor data coverage.

The use of a 99% confidence level VaR statistic does not provide information about losses beyond this level, usually referred to as 'tail' risks. These risks are more appropriately assessed using measures such as SVaR and stress testing.

The use of a one-day time horizon does not fully capture the profit and loss implications of positions that cannot be liquidated or hedged within one day. This may not fully reflect market risk at times of severe illiquidity in the market when a one-day period may be insufficient to liquidate or hedge positions fully. Thus, the regulatory VaR that is used for modelled market risk capital uses a ten-day time horizon.

Finally, volatile market conditions, such as those experienced in 2015, can lead to new risk factors emerging. This issue is addressed by using a combination of proxy risk factors and the RNIV framework to supplement the VaR model.

*unaudited

Market risk continued

1-day 99% traded internal VaR*

The table below analyses internal VaR for the trading portfolios of RBS plc and RBSSI, segregated by type of market risk exposure.

	2015				2014			
RBS plc	Average £m	Period end £m	Maximum £m	Minimum £m	Average £m	Period end £m	Maximum £m	Minimum £m
Interest rate	14.6	12.5	26.7	9.7	16.1	18.5	35.6	9.7
Credit spread	10.3	7.4	16.4	6.4	21.4	14.4	38.3	13.8
Currency	5.3	5.2	9.1	1.9	5.0	6.5	9.5	1.4
Equity	1.6	0.8	6.0	0.4	3.0	3.6	6.4	1.2
Commodity	0.4	0.5	2.2	0.2	0.6	0.4	2.5	0.3
Diversification (2)		(9.4)				(22.7)		
Total	19.0	17.0	30.5	13.1	26.5	20.7	55.8	16.9

	2015				2014			
RBSSI	Average (1) £m	Period end £m	Maximum (1) £m	Minimum £m	Average £m	Period end £m	Maximum £m	Minimum £m
Interest rate	2.3	2.3	6.0	0.9	6.4	3.0	14.5	1.6
Credit spread	1.3	0.8	2.8	0.8	10.2	2.7	17.6	2.7
Currency	—	—	—	—	0.1	—	0.2	—
Equity	0.2	—	0.4	—	0.3	0.3	0.8	0.2
Commodity	0.3	—	0.5	0.1	0.1	—	0.5	—
Diversification (2)		(1.9)				(4.1)		
Total	1.3	1.2	3.2	0.6	7.4	1.9	18.1	1.4

Notes:
(1) The average and maximum currency and total VaR for 2015 have been adjusted to reflect genuine maximum exposures.
(2) RBS plc benefits from diversification as it reduces risk by allocating positions across various financial instrument types, currencies and markets. The extent of the diversification benefit depends on the correlation between the assets and risk factors in the portfolio at a particular time. The diversification factor is the sum of the VaR on individual risk types less the total portfolio VaR.

Key points

RBS plc

- Total traded VaR decreased in 2015, falling by 18% on a period end basis and by 28% on an average basis. This reflected the continued alignment of the trading business with RBS Group strategy. A notable driver was the decrease in credit spread VaR reflecting the exit from a significant part of US asset-backed product (ABP) trading in the first half of 2015.
- VaR remained volatile, reflecting developments in the eurozone periphery, evolving geopolitical risks - notably, developing tensions in the Middle East and in Russia and Ukraine - and a number of other macroeconomic factors. These included, but were not limited to, the Swiss central bank's unexpected removal of the Swiss franc's peg to the euro in January and growing concerns regarding economic slowdown in China.

RBSSI

- Total traded VaR declined, by 37% on a period end basis and by 82% on an average basis, driven by the same overall factor as for RBS plc.

*unaudited

VaR validation*

Quantitative analysis is used to:

- Perform internal back-testing to complement the regulatory back-testing; and
- Identify risks not adequately captured in VaR, and ensure that such risks are addressed via the RNIV framework (refer to page 125).

In addition, as part of ongoing risk management, any market or portfolio weaknesses that could become significant are identified.

The VaR model is also subject to independent reviews carried out by Model Risk Management (refer to page 33).

As well as being an important market risk measurement and control tool, the VaR model is also used to determine a significant component of the market risk capital requirement (refer to page 126 for more information on calculation of capital requirements). Therefore, it is subject to not only ongoing internal review and validation but also regulator-prescribed back-testing.

VaR back-testing*

The main approach employed to assess the ongoing performance of the VaR model is back-testing, which counts the number of days when a loss exceeds the corresponding daily VaR estimate, measured at a 99% confidence level.

Two types of profit and loss (P&L) are used in back-testing comparisons: Actual P&L and Hypothetical (Hypo) P&L.

The Actual P&L for a particular business day is the firm's actual P&L for that day in respect of the trading activities within the scope of the firm's regulatory VaR model, including any intraday activities, adjusted by stripping out fees and commissions, brokerage, and additions to and releases from reserves that are not directly related to market risk.

The Hypo P&L reflects the firm's Actual P&L excluding any intra-day activities.

A portfolio is said to produce a back-testing exception when the Actual or Hypo P&L exceeds the VaR level on a given day. Such an event may be caused by a large market movement or may highlight issues such as missing risk factors or inappropriate time series. Any such issues identified are analysed and addressed through taking appropriate remediation or development action. The RBS Group monitors both Actual and Hypo back-testing exceptions.

Back-testing at the legal entity level is performed and reported on 1-day 99% regulatory VaR. Back-testing at the franchise level and lower-level portfolios is performed on 1-day 99% internal VaR.

*unaudited

Market risk continued

The graph below presents 1-day 99% regulatory VaR vs. Actual and Hypo P&L for RBS plc.

The table below shows regulatory back-testing exceptions for a period of 250 business days for 1-day 99% traded regulatory VaR vs. Actual and Hypo P&L for the legal entities approved by the PRA.

Description	Back-testing exceptions		Model status
	Actual	Hypo	
The Royal Bank of Scotland plc (1)	4	3	Green
National Westminster Bank Plc	9	7	Amber
RBS Securities Inc (RBSSI)	4	3	Green
RBS Financial Products Inc	—	—	Green

Note:
(1) A waiver was obtained for the RBS plc exception (Actual and Hypo) on 22 June 2015 as it was considered to be of a technical nature. Therefore, this exception is not included in the table above.

Key points

- Statistically the Group would expect to see back-testing exceptions 1% of the time over a period of 250 business days. From a capital requirement perspective, the PRA categorises a firm's VaR model as green, amber or red. A green model status is consistent with a satisfactory VaR model and is achieved for models that have four or fewer exceptions in a continuous 250-day period. An amber model status suggests potential issues regarding the quality or accuracy of the model in question but no definitive conclusions.
- Most of the back-testing exceptions experienced in the period were driven by the higher market volatility and reduced liquidity.
- The exceptions in RBS plc resulted from losses in the Rates business due to the rates sell-off and steepening across the euro and sterling curves between May and August. In addition, the exception on 31 December 2015 was due to various valuation adjustments carried out at the year end to re-mark the prices of certain trades.
- NatWest Plc experienced nine exceptions during the period. There is normally a back-to-back arrangement with RBS plc. However, on the dates when the exceptions occurred, the residual risk at end of the day resulted in the exceptions due to the business being adversely positioned to market moves.
- The exceptions in RBSSI resulted from losses in the US Rates business due to adverse rate movements, losses on the sale of positions from Capital Resolution and the sell-down of residual equity positions as part of disposal strategy.

Stressed VaR (SVaR)*

As with VaR, the SVaR technique produces estimates of the potential change in the market value of a portfolio, over a specified time horizon, at a given confidence level. SVaR is a VaR-based measure using historical data from a one-year period of stressed market conditions.

The risk system simulates 99% VaR on the current portfolio for each 250-day period from 1 January 2005 to the current VaR date, moving forward one day at a time. The SVaR is the worst VaR outcome of the simulated results.

This is in contrast with VaR, which is based on a rolling 500-day historical data set. For the purposes of both internal risk management and regulatory SVaR calculation, a time horizon of ten trading days is assumed with a confidence level of 99%.

The internal traded SVaR model captures all trading book positions, including not only those products, locations and legal entities approved by the regulator.

Risks not in VaR (RNIVs)*

The RNIV approach is used for market risks that are insufficiently captured by the VaR and SVaR model methodologies, for example due to a lack of suitable historical data. The RNIV framework has been developed to quantify these market risks and to ensure that the RBS Group holds adequate capital.

The need for an RNIV calculation is typically identified in one of the following two circumstances: (i) as part of the New Product Risk Assessment process, when a risk manager assesses that the associated risk is not adequately captured by the VaR model; or (ii) as a result of a recommendation made by Model Risk Management or the model validation team when reviewing the VaR model.

The RNIV calculations provide a capital estimate of risks not captured in the VaR model and are regularly reported and discussed with senior management and the regulator. The methodology used in the material RNIV calculations is internally reviewed by Model Risk. Where appropriate, risk managers set sensitivity limits to control specific risk factors giving rise to the RNIV. RNIV calculations form an integral part of the RBS Group's ongoing model and data improvement efforts to capture all market risks in scope for model approval in VaR and SVaR.

The Group adopts two approaches for the quantification of RNIVs:

- A VaR/SVaR approach. Under this approach, two values are calculated: (i) the VaR RNIV; and (ii) the SVaR RNIV.
- A stress-scenario approach. Under this approach, an assessment of ten-day extreme, but plausible, market moves is used in combination with position sensitivities to give a stress-type loss number - the stress-based RNIV value.

For each legal entity covered by the PRA VaR approval (refer to Regulatory VaR), RNIV amounts are aggregated to obtain the following three measures: (i) Total VaR RNIV; (ii) Total SVaR RNIV; and (iii) Total stress-based RNIV. In each of these categories, potential diversification benefits between RNIVs are ignored.

Stress testing*

The RBS Group undertakes daily market risk stress testing to identify vulnerabilities and potential losses in excess of or not captured in VaR. The calculated stresses measure the impact of changes in risk factors on the fair values of the trading and available-for-sale portfolios.

The RBS Group conducts historical, macroeconomic and vulnerability-based stress testing.

Scenario-based sensitivity analysis measures the sensitivity of the current portfolio to defined movements in market risk factors. These risk factor movements and the resulting valuation changes are typically smaller than those considered in other stress tests.

Historical stress testing is a measure that is used for internal management. Using the historical simulation framework used for VaR, the current portfolio is stressed using historical data since 1 January 2005. The methodology simulates the impact of the 99.9 percentile loss that would be incurred by historical risk factor movements over the period, assuming variable holding periods specific to the risk factors and the businesses.

Historical stress tests form part of the market risk limit framework and their results are reported daily to senior management

Macroeconomic stress tests are carried out periodically as part of the firm-wide, cross-risk capital planning process. The scenario narratives are translated into risk factor shocks using historical events and insights by economists, risk managers and the front office. Market risk stress results are combined with those for other risks into the capital plan that is presented to the Board. The cross-risk capital planning process is conducted twice a year, in April/May and October/November, with a planning horizon of five years. The scenario narratives cover both regulatory scenarios and macroeconomic scenarios identified by the firm.

Vulnerability-based stress testing begins with the analysis of a portfolio and expresses the key vulnerabilities of the portfolio in terms of plausible, so-called vulnerability scenarios under which the portfolio would suffer material losses. These scenarios can be historical, macroeconomic or forward-looking/hypothetical. Vulnerability-based stress testing is used for internal management information and is not subject to limits. However, relevant scenarios are reported to senior management.

*unaudited

Market risk continued

Economic capital*

The market risk economic capital framework uses models to calculate the market and default risk in the trading book which are aligned with other models that are used for limit setting and market risk management. The results are annualised to be consistent with the other economic capital models to permit consolidation of all risk types as part of the RBS Group-wide economic capital programme.

Market risk regulatory capital*

Regulatory treatment

The market risks subject to capital requirements under Pillar 1 are primarily interest rate, credit spread and equity risks in the trading book and foreign exchange and commodity risks in both the trading and non-trading books. Interest rate and equity risks are split between general and specific risks. General risks represent market risks due to a move in a market as a whole, such as a main index or yield curve, while specific risks represent market risks arising from events particular to an underlying issuer.

The Group uses two broad methodologies to calculate its market risk capital charge: (i) the non-modelled approach, whereby regulator-prescribed rules are applied, and (ii) the internal model approach, where, subject to regulatory approval, a model such as VaR is used to calculate the capital charge.

VaR and SVaR capture general and specific risks but not risks arising from the impact of defaults and rating changes associated with traded credit products and their derivatives. For these risks, two product-dependent approaches are used:

- The incremental risk charge (IRC) model captures risks arising from rating migration and default events for the more liquid traded credit instruments and their derivatives.
- Securitisation and re-securitisation risks in the trading book are treated with the non-trading book non-modelled capitalisation approach.

Regulatory VaR

The Group's VaR model has been approved by the PRA to calculate its regulatory market risk capital requirement for the trading book for those legal entities under its jurisdiction. These legal entities are RBS plc, NatWest Plc, RBS Securities Inc and RBS Financial Products Inc.

While internal VaR provides a measure of the economic risk, regulatory VaR is one of the measures of regulatory capital requirements by legal entity.

The calculation of regulatory VaR differs from that of the internal VaR as it takes into account only regulator-approved products, locations and legal entities and it is based on a ten-day, rather than a one-day, holding period for market risk capital calculations.

The PRA approval covers general market risk in interest rate, foreign exchange, equity and commodity products and specific market risk in interest rate and equity products.

Regulatory SVaR*

The Group's SVaR model has also been approved by the PRA for use in the capital requirement calculation. The distinction between regulatory SVaR and internal SVaR is the same as that between regulatory VaR and internal VaR.

Risks not in VaR

As discussed earlier, the RNIV framework ensures that the risks not captured in VaR are adequately covered by capital.

Incremental risk charge (IRC)*

The IRC model quantifies the impact of rating migration and default events on the market value of instruments with embedded credit risk (in particular, bonds and credit default swaps) that are held in the trading book. It further captures basis risk between different instruments, maturities and reference entities. Following the internal ratings-based approach for credit risk, the IRC is calculated over a one-year capital horizon with a 99.9% confidence level. The dependency of positions is modelled using a single-factor Gaussian copula.

The IRC is mainly driven by three-month credit rating transition, default and correlation parameters. The portfolio impact of correlated defaults and rating changes is assessed by observing changes in the market value of positions using stressed recovery rates and modelled credit spread changes. Revaluation matrices are used to capture any non-linear behaviour.

*unaudited

Market risk capital*

Minimum capital requirements

The following table analyses total market risk minimum capital requirements for RBS plc and RBSSI at 31 December 2015, calculated in accordance with the Capital Requirements Regulation (CRR). The minimum capital requirements represent 8% of the corresponding RWA amounts.

	2015		2014	
	RBS plc £m	RBSSI £m	RBS plc £m	RBSSI £m
Interest rate position risk requirement	55	9	74	16
Equity position risk requirement	—	1	—	1
Option position risk requirement	1	—	1	—
Foreign currency position risk requirement	131	—	52	—
Specific interest rate risk of securitisation positions	130	1	243	27
Total (non-modelled approach)	317	11	370	44
Pillar 1 model based position risk requirement	1,209	62	1,148	213
Total market risk minimum capital requirement	1,526	73	1,518	257

*unaudited

Market risk continued

The following table analyses the principal contributors to the Pillar 1 model based position risk requirements (PRRs) presented in the previous table.

	2015				2014
	Average	Maximum	Minimum	Period end	Period end
RBS plc	£m	£m	£m	£m	£m
Value-at-risk	323	365	283	350	267
Stressed VaR	397	421	361	412	338
Incremental risk charge	254	303	229	230	240
Risk not in VaR	251	305	215	217	303
Total				1,209	1,148
RBSSI					
Value-at-risk	13	25	10	10	35
Stressed VaR	59	70	33	33	108
Incremental risk charge	18	40	11	15	54
Risk not in VaR	10	18	4	4	16
Total				62	213

Key points

RBS plc

- The total market risk minimum capital requirement was broadly unchanged at 31 December 2015, with a moderate decrease in the standard or non-modelled component being offset by an increase in the Pillar 1 model-based component.
- The decrease in the non-modelled PRR was largely driven by a decline in trading book securitisation positions as a result of asset disposals, in line with the wind-down of the US ABP business. This was partially offset by an increase in the foreign currency PRR, reflecting the sale of Citizens, which led to an increase in the US dollar capital position.
- The rise in the Pillar 1 model-based PRR was primarily driven by increases in the VaR and SVaR charges, reflecting risk increases across the Rates business, primarily related to the European and US swap portfolios and the US options business. This was offset partly by a decrease in the RNIV charge, primarily in stress-based RNIV reflecting ongoing improvements in the capture of risks in the RNIV framework.

RBSSI

- The total market risk minimum capital requirement fell significantly during 2015, chiefly reflecting de-risking strategy.
- The decline in the non-modelled component primarily reflected reductions in trading book securitisation positions.
- The decline in all Pillar 1 model-based charges was principally driven by the wind-down and exit from the US mortgage business, which is now largely complete, a large reduction in the flow credit trading business and a general risk reduction in the US rates business.

Valuation and independent price verification

Traders are responsible for marking-to-market their trading book positions daily, ensuring that assets and liabilities in the trading book are measured at their fair value. Any profits or losses on the revaluation of positions are recognised daily.

Product controllers are responsible for ensuring that independent price verification processes are in place covering all trading book positions held by their business. Independent price verification and trader supervision are the key controls over front office marking of positions.

Model validation*

The Group uses a variety of models to manage and measure market risk. These include pricing models (used for valuation of positions) and risk models (for risk measurement and capital calculation purposes). They are developed in both RBS Group-level and lower-level functions and are subject to independent review and sign-off.

For general information on the independent model validation carried out by Model Risk Management (MRM), which applies also to market risk models (including VaR), refer to page 33. Additional details relating to pricing and market risk models are presented below.

Pricing models

Pricing models are developed by a dedicated front office quantitative team, in conjunction with the trading desk. They are used for the valuation of positions for which prices are not directly observable and for the risk management of the portfolio.

Any pricing models that are used as the basis for valuing books and records are subject to approval and oversight by asset-level modelled product review committees.

These committees comprise representatives of the major stakeholders in the valuation process - trading, finance, market risk, model development and model review functions.

The review process comprises the following steps:

- The committees prioritise models for review by MRM, considering the materiality of the risk booked against the model and an assessment of the degree of model risk, that is the valuation uncertainty arising from the choice of modelling assumptions.
- MRM quantifies the model risk by comparing front office model outputs with those of alternative models independently developed by MRM.
- The sensitivities derived from the pricing models are validated.
- The conclusions of the review are used by MRM to inform risk limits and by Finance to inform model reserves.

Risk models

All model changes are approved through model governance committees at franchise level. Changes to existing models that have an impact on VaR exceeding 5% at legal entity level or 15% at a major business level are also subject to MRM review and sign-off as are all model changes that require regulator approval before implementation.

MRM's independent oversight provides additional assurance that the RBS Group holds appropriate capital for the market risk to which it is exposed.

In addition to MRM's independent oversight, the model testing team monitors the model performance for market risk through back-testing, which is discussed in more detail on page 123, and other processes.

Non-traded market risk

Risk governance

The RBS Group manages the three key categories of non-traded market risk separately. The categories are: non-traded interest rate risk; non-traded foreign exchange risk; and non-traded equity risk.

The Chief Risk Officer delegates responsibility for day-to-day control of non-traded market risk to the Director of Market Risk.

Non-traded market risk positions are reported to the ALCo and the Board, monthly in the case of interest rate risk and quarterly in the case of foreign exchange and equity risk.

The Executive Risk Forum (ERF) approves the non-traded market risk framework. The non-traded market risk policy statement sets out the governance and risk management framework through effective identification, measurement, reporting, mitigation, monitoring and control.

The key models used for managing non-traded market risk benefit from the validation process described on this page.

Risk assessment, monitoring and mitigation

Interest rate risk*

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

- Repricing risk - which arises when asset and liability positions either mature (in the case of fixed-rate positions) or their interest rates reset (in the case of floating-rate positions) at different dates. These mismatches may give rise to net interest income and economic value volatility as interest rates vary.
- Yield curve risk - which arises from unanticipated changes in the shape of the yield curve, such that rates at different maturity points may move differently. Such movements may give rise to interest income and economic value volatility.
- The two risk factors above incorporate the duration risk arising from the reinvestment of maturing swaps hedging net free reserves (or net exposure to equity and other low fixed-rate or non-interest-bearing liability balances including, but not limited to, current accounts).

*unaudited

Market risk continued

- Basis risk - which arises when related instruments with the same tenor are valued using different reference yield curves. Changes in the spread between the different reference curves can result in unexpected changes in the valuation of or income difference between assets, liabilities or derivative instruments. This occurs, for example, in the retail and commercial portfolios, when products valued on the basis of the Bank of England base rate are funded with LIBOR-linked instruments.
- Optionality risk - which arises when customers have the right to terminate, prepay or otherwise alter a transaction without penalty, resulting in a change in the timing or magnitude of the cash flows of an asset, liability or off-balance sheet instrument.

Due to the long-term nature of many non-trading book portfolios and their varied interest rate repricing characteristics and maturities, it is likely that net interest income will vary from period to period, even if interest rates remain the same. New business originated in any period will alter the RBS Group's interest rate sensitivity if the resulting portfolio differs from portfolios originated in prior periods, depending on the extent to which exposure has been hedged.

The RBS Group's policy is to manage the interest rate sensitivity within risk limits that are approved by the ERF and endorsed by the ALCo before being cascaded to lower levels. These include, in particular, interest rate sensitivity and VaR limits.

In order to manage exposures within these limits, the RBS Group aggregates its interest rate positions and hedges them externally using cash and derivatives - primarily interest rate swaps.

This task is primarily carried out by RBS Group Treasury, to which all businesses except CIB transfer most of their NTIRR. The main exposures and limit utilisations are reported to the RBS Group ALCo and the RBS Group Board monthly.

Foreign exchange risk

The only material non-traded open currency positions are the structural foreign exchange exposures arising from investments in foreign subsidiaries, branches and associates and their related currency funding. These exposures are assessed and managed by RBS Group Treasury to predefined risk appetite levels under delegated authority from the ALCo. RBS Group Treasury seeks to limit the potential volatility impact on the RBS Group's Common Equity Tier 1 (CET1) ratio from exchange rate movements by maintaining a structural open currency position. Gains or losses arising from the retranslation of net investments in overseas operations are recognised in equity reserves and reduce the sensitivity of capital ratios to foreign exchange rate movements primarily arising from the retranslation of non-sterling-denominated RWAs. Sensitivity is minimised where, for a given currency, the ratio of the structural open position to RWAs equals the RBS Group's CET1 ratio. The sensitivity of the CET1 capital ratio to exchange rates is monitored monthly and reported to the ALCo at least quarterly.

Foreign exchange exposures arising from customer transactions are sold down by businesses on a regular basis in line with RBS Group policy.

Equity risk

Non-traded equity risk is the potential variation in the income and reserves arising from changes in non-trading book equity valuations. Any such risk is identified prior to any investments and then mitigated through a framework of controls.

Investments, acquisitions or disposals of a strategic nature are referred to the RBS Group's Acquisitions and Disposals Committee (ADCo). Once approved by ADCo for execution, such transactions are referred for approval to the RBS Group Board, the RBS Group Executive Committee, the RBS Group Chief Executive Officer, the RBS Group Chief Financial Officer or as otherwise required. Decisions to acquire or hold equity positions in the non-trading book that are not of a strategic nature, such as customer restructurings, are taken by authorised persons with delegated authority under the credit approval framework.

Risk measurement

Interest rate risk*

NTIRR can be measured from either an economic value-based or earnings-based perspective (or both). Value-based approaches measure the change in value of the balance sheet assets and liabilities over a longer timeframe, including all cash flows. Earnings-based approaches measure the potential short-term (generally one year) impact on the income statement of charges in interest rates.

The RBS Group uses both approaches to quantify its interest rate risk: VaR as its value-based approach and sensitivity of net interest income (NII) as its earnings-based approach.

These two approaches provide different yet complementary views of the impact of interest rate risk on the balance sheet at a point in time. The scenarios employed in the NII sensitivity approach incorporate business assumptions and simulated modifications in customer behaviour as interest rates change. In contrast, the VaR approach assumes static underlying positions and therefore does not provide a dynamic measurement of interest rate risk. In addition, while the NII sensitivity calculations are measured to a 12 month horizon and thus provide a shorter-term view of the risks on the balance sheet, the VaR approach can identify risks not captured in the sensitivity analysis, in particular the impact of duration and repricing risk on earnings beyond 12 months.

NII sensitivity is calculated and monitored at RBS Group level.

*Value-at-risk**

The Group's standard VaR metrics - which assume a time horizon of one trading day and a confidence level of 99% - are based on interest rate repricing gaps at the reporting date. Daily rate moves are modelled using observations over the last 500 business days. These incorporate customer products plus associated funding and hedging transactions as well as non-financial assets and liabilities such as property, plant and equipment, capital and reserves. Behavioural assumptions are applied as appropriate.

*unaudited

The table below shows the NTIRR VaR for the Group's retail and commercial banking activities at a 99% confidence level together with a currency analysis of period end VaR. It captures the risk resulting from mismatches in the repricing dates of assets and liabilities. This includes any mismatch between structural hedges and stable non and low interest bearing liabilities such as equity and money transmission accounts as regards their interest rate repricing behavioural profile.

	Average £m	Period end £m	Maximum £m	Minimum £m
2015 - excluding Citizens	36	20	65	12
2015 - Citizens	5	—	16	—
2015 - total	32	20	68	12
2014 - excluding Citizens	82	61	104	53
2014 - Citizens	20	11	42	8
2014 - total	96	72	132	66

		2014		
Period end VaR	2015 £m	Excluding Citizens £m	Citizens £m	Total £m
Euro	8	1	—	1
Sterling	18	24	—	24
US dollar	4	37	11	48
Other	4	3	—	3

Key points

- The Group's average VaR was higher than that of RBS Group as some structural interest rate exposures were hedged at a consolidated level.
- Average interest rate VaR was lower in 2015 as the Group steered its structural interest rate exposure more closely to the neutral duration prescribed by its internal risk management policy.
- The main movement by currency in 2015 relates to US dollar where VaR declined due to the disposal of Citizens.

Market risk continued

Foreign exchange risk

The Group does not maintain material non-traded open currency positions other than the structural foreign currency translation exposures arising from its investments in foreign subsidiaries and associated undertakings and their related currency funding.

The table below shows the Group's structural foreign currency exposures.

2015	Net assets of overseas operations £m	Non-controlling interests (NCI) £m	Net assets of overseas operations excluding NCI £m	Net investment hedges £m	Structural foreign currency exposures £m
US dollar	359	—	359	(7)	352
Euro	5,234	—	5,234	(573)	4,661
Swiss franc	797	—	797	(711)	86
Other non-sterling	1,035	—	1,035	(602)	433
	7,425	—	7,425	(1,893)	5,532
2014					
US dollar - excluding Citizens	2,627	—	2,627	(700)	1,927
US dollar - Citizens	7,868	(2,321)	5,547	(2,013)	3,534
US dollar - total	10,495	(2,321)	8,174	(2,713)	5,461
Euro	3,935	—	3,935	(184)	3,751
Swiss franc	930	—	930	(902)	28
Other non-sterling	1,406	—	1,406	(898)	508
	16,766	(2,321)	14,445	(4,697)	9,748

Key points

- The Group's structural foreign currency exposure at 31 December 2015 was £5.5 billion, a decrease of £4.2 billion from the end of 2014.
- The reduction in exposure was largely due to the disposal of Citizens, which reduced net assets by £7.9 billion, NCI by £2.3 billion and hedges by £2.0 billion.
- Other key movements during the year included a £2.0 billion reduction in US dollar-denominated net assets relating to litigation provisions, partly offset by a £1.3 billion increase in euro-denominated net assets, mainly contributed by Ulster Bank RoI.
- Changes in foreign currency exchange rates affect equity in proportion to structural foreign currency exposure. For example, a 5% strengthening or weakening in foreign currencies against sterling would result in a gain or loss of £0.3 billion in equity, respectively (2014 - £0.5 billion).

1-day 99% internal VaR for non-trading book (primarily CIB and Capital Resolution)*

The table below analyses 1-day 99% internal VaR for RBS plc's non-trading books in CIB and Capital Resolution. Other than the structured credit portfolio, these books do not typically form part of the structural interest rate framework due to the short-term nature of the interest rate risks they carry. They are therefore monitored and managed through the same framework and using the same metrics as portfolios in the trading book.

	2015				2014			
	Average £m	Period end £m	Maximum £m	Minimum £m	Average £m	Period end £m	Maximum £m	Minimum £m
Interest rate	1.4	0.8	2.2	0.7	1.8	1.8	5.5	1.1
Credit spread	1.0	0.6	2.7	0.5	2.8	2.4	4.1	1.7
Currency	0.2	0.2	2.1	—	0.3	0.4	0.7	—
Diversification (1)		(0.7)				(1.9)		
Total	1.7	0.9	2.9	0.9	3.2	2.7	6.4	2.0

Notes:
(1) RBS plc benefits from diversification as it reduces risk by allocating positions across various financial instrument types, currencies and markets. The extent of the diversification benefit depends on the correlation between the assets and risk factors in the portfolio at a particular time. The diversification factor is the sum of the VaR on individual risk types less the total portfolio VaR.
(2) The table above excludes the structured credit portfolio and loans and receivables.

Key point

- The average VaR for RBS plc's non-trading book, predominantly comprising available-for-sale portfolios, declined in 2015 compared with 2014. This was largely driven by a decline in the credit spread VaR as a result of (i) Capital Resolution run-down, and (ii) the transfer of collateral and money market non-trading books into Treasury.

*unaudited

Market risk continued

1-day 99% internal VaR for non-trading book (Treasury)*

The interest rate risk and credit spread risk in Treasury arise primarily from portfolios held for liquidity and collateral management purposes. Credit spread risk is the risk arising from the volatility in the spread between bond and swap rates and arises mainly from those non-trading book debt securities that are accounted at fair value. This risk is reflected through changes in the portfolio valuation and is recognised in capital through available-for-sale (AFS) reserves.

The table below shows the Group's interest rate and credit spread VaR relating to these exposures.

	2015 £m
Interest rate	2.8
Credit spread	30.8

Note:
(1) Interest rate exposure managed outside the structural interest rate exposure process.

Structured credit portfolio

The Group's structured credit portfolio is measured on a notional and fair value basis due to its illiquid nature. Notional and fair value decreased to £39 million and £49 million respectively (2014 - £0.4 billion and £0.3 billion), reflecting the sale of underlying assets, primarily collateralised loan obligations, in line with Capital Resolution strategy.

Calculation of regulatory capital*

The RBS Group holds capital for two types of non-traded market risk exposures: NTIRR and non-trading book foreign exchange.

Capital for NTIRR is captured under the Pillar 2A process. This is calculated by considering the potential impact on the RBS Group's economic value over a one year horizon. The four main sources of NTIRR - repricing, yield curve, basis and optionality risks - are captured in the calculation.

Pillar 1 capital must be held for non-trading book foreign exchange exposures, as outlined under CRR Articles 455 and 92(3)c. Structural foreign exchange exposures are excluded from the calculations as outlined under CRR Article 352(2); such exposures are considered under Pillar 2A.

Non-traded equity risk is captured in credit risk RWAs.

The capital calculations under ICAAP are also used for economic capital purposes.

*unaudited

Report of the directors

The directors present their report together with the audited accounts for the year ended 31 December 2015.

Group structure

The Royal Bank of Scotland plc (the 'Bank') is a wholly-owned subsidiary of The Royal Bank of Scotland Group plc (the 'holding company'), which is incorporated in Great Britain and has its registered office at 36 St Andrew Square, Edinburgh EH2 2YB. The 'Group' comprises the Bank and its subsidiary and associated undertakings. Details of the principal subsidiary undertakings and their activities are shown in Note 15 on the accounts. A full list of related undertakings of the company is shown in Note 41 on the accounts. 'RBS Group' comprises the holding company and its subsidiary and associated undertakings.

The financial statements of The Royal Bank of Scotland Group plc can be obtained from RBS Secretariat, RBS Gogarburn, Edinburgh, EH12 1HQ, the Registrar of Companies or through the RBS Group's website rbs.com

Following placing and open offers in December 2008 and in April 2009, HM Treasury (HMT) owned approximately 70.3% of the enlarged ordinary share capital of the holding company. In December 2009, the holding company issued a further £25.5 billion of new capital to HMT in the form of B shares. HMT sold 630 million of its holding of the holding company's ordinary shares in August 2015. In October 2015 HMT converted its entire holding of 51 billion B shares into 5.1 billion new ordinary shares of £1 each in the holding company.

At 31 December 2015, HMT's holding in the holding company's ordinary shares was 72.6%.

RBS Holdings N.V. (formerly ABN AMRO Holding N.V.)

In 2007, RFS Holdings B.V., which was jointly owned by RBS, the Dutch State (successor to Fortis) and Santander completed the acquisition of ABN AMRO Holding N.V.

Following the announcements in April 2011 by the Boards of RBSG, RBS plc, RBS Holdings and RBS N.V., a substantial part of the business activities of RBS N.V. had been successfully transferred to RBS plc by the end of 2012, with further transfers in 2013 and 2014. There have been no transfers in 2015, the focus continues to be on further de-risking the RBS N.V. balance sheet.

Results and dividends

The loss attributable to the ordinary shareholders of the Bank for the year ended 31 December 2015 amounted to £1,950 million compared with a loss of £3,234 million for the year ended 31 December 2014, as set out in the consolidated income statement on page 142.

The Bank did not pay a dividend on ordinary shares in 2015, 2014, or 2013.

Strategic report

Activities

The Group is engaged principally in providing a wide range of banking and other financial services. Further details of the organisational structure and business overview of the Group, including the products and services provided by each of its segments, are contained in the Financial review on pages 3 to 5.

Risk factors

The Group's future performance and results could be materially different from expected results depending on the outcome of certain potential risks and uncertainties. Full details of these and other risk factors are set out on pages 268 to 293.

The reported results of the Group are also sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Details of the Group's critical accounting policies and key sources of accounting judgments are included in Accounting policies on pages 148 to 162.

The Group's approach to risk management, including its financial risk management objectives and policies and information on the Group's exposure to price, credit, liquidity and cash flow risk, is discussed in the Capital and risk management section of the Financial review on pages 28 to 134.

Financial performance

A review of the Group's performance during the year ended 31 December 2015, including details of each operating segment, and the Group's financial position as at that date is contained in the Financial review on pages 6 to 27.

Employees

Policies and practices in respect of employee issues are managed on a consistent basis across the RBS Group, and the following sections reflect this approach.

As at 31 December 2015, the Bank and its subsidiaries employed 87,000 employees (full time equivalent basis) throughout the world. Details of employee related costs are included in Note 3 on the accounts.

Living our values

Our values, introduced in 2012, guide our actions every day, in every part of our business. They are at the heart of the way we work. They are embedded within our behavioural frameworks - this means the way we recruit, promote, reward and manage our people are all aligned.

Building a healthy culture and risk culture that lives up to our values is one of our core priorities. We have governance to monitor and guide and track progress on our cultural goals. We gather qualitative and quantitative feedback to assess our progress and respond accordingly. We do this in tandem with feedback from regulators and industry bodies

Engaging our people

We recognise that building an engaged, healthy and inclusive workforce is crucial if we are to achieve our ambition. We continue to ask people across the Bank to share their thoughts on what it's like to work at RBS Group via our annual employee survey (OurView).

The results enable our people leaders to monitor levels of engagement and work with their teams to make improvements. It also enables us to monitor employee perception and the progress we are making versus our goals. Our most recent survey, in which more than 62,000 colleagues took part, showed significant improvement in employee engagement and leadership.

In 2015 we launched determined to make a difference, an internal campaign that provides a rallying call for our employees. It was drawn from our extensive research with staff and is based on their reflections about the difference we make for our customers, colleagues, communities and shareholders.

Rewarding our people

Our approach to performance management allows us to provide clarity for our people about how their individual contribution links to our ambition. It recognises behaviour that supports our values and holds individuals to account for behaviour and performance that does not.

In the UK we are a living wage employer meaning that we adhere to Living Wage Benchmarks (both national and London) for all employees. All third party contractors who regularly work in our buildings will also be in scope by 2017 at the latest.

In 2015, we announced the removal of incentive schemes for our customer facing employees in Personal & Business Banking. Instead, we gave every eligible employee an increase to their guaranteed pay. This change ensures that our people are paid clearly, fairly and simply for the job they do for our customers every day. It also ensures our customers can be certain that if they take a product from us, it has no financial impact on what our people are paid.

Youth employment

We have hired over 250 graduates and over 300 Apprentices in 2015. We have been accredited by "Investors in Young People" for how we attract, recruit and develop our talent.

Health and wellbeing of our people

We offer a wide range of health benefits and services to help maintain physical and mental health, and support our people if they become unwell.

In 2015, our wellbeing programme focused on three main areas; Mental Health, Physical Health and Resilience. Activities include the continued promotion of Lifematters (RBS Group's Employee Assistance Programme), participation in the Global Corporate Challenge, the launch of Resilience programmes and continued support for Time to Change, the UK's biggest programme to challenge mental health stigma.

Employee consultation

We recognise employee representatives such as trade unions and work councils in a number of businesses and countries. There has been ongoing engagement and discussion with those bodies given the changes the bank announced in February 2015. Management have continued to meet regularly with our European Employee Council to discuss developments and update on the progress of our strategic plans.

Inclusion

Building a more inclusive bank is essential for our customers and colleagues. Our inclusion policy standard applies to all our people globally.

During 2015 we continued our roll out of unconscious bias learning for all employees. We've introduced a gender goal to have at least 30% of women in the bank's top three leadership levels by 2020. Further, we aim to have 50/50 balance at all levels by 2030. This is supported by the launch of a female development proposition. An increased focus on disability has led to the development of a comprehensive plan to support our colleagues and customers with additional needs and will help RBS Group achieve its ambition of becoming a 'disability smart' organisation. From an LGBT perspective, we continue to deliver improvements to our people policies and customer operating procedures, including the introduction of guidance to support employees going through gender transition, introducing the 'Mx' honorific, and improving our customer gender change process. We are finalising plans to improve our ethnic representation within senior roles and are continuing to support our 15,000 strong employee-led networks.

RBS Group has been recognised for its work on Equality, Diversity and Inclusion by our Platinum ranking from Opportunity Now (gender) - our Gold ranking for Race for Opportunity (race); retaining a position in the Times Top 50 Employers for Women; and improving upon our ranking in the Stonewall Workplace Equality Index (LGBT).

Sustainability

Sustainability at RBS Group means building our business around long term thinking and support for our customers and the communities in which they live. Our core responsibility is to obey the law and to ensure that our business is built on safe and secure financial foundations, and we have worked hard in the years since the financial crisis to achieve this position. This underpins everything that RBS Group does and enables people to run their daily lives and businesses. Our position as a provider of credit supports economic growth and brings wider benefits to society.

But our ambition is to go further, to shape the world around us in a positive way. We recognise that we still have a long way to go achieve this position across our business. Sustainability is therefore not just about the many responsibilities and obligations that RBS Group has, but about taking leadership on a broad range of issues that are important to our Stakeholders.

The Sustainable Banking Committee is responsible for overseeing and challenging how management is addressing sustainable banking and reputation issues, considering the long term interests of all stakeholder groups.

For more information on our approach and progress read the RBS Group Sustainability Report, available on rbs.com/sustainable.

Going concern

The Group's business activities and financial position, the factors likely to affect its future development and performance and its objectives and policies in managing the financial risks to which it is exposed and its capital are discussed in the Financial review. The risk factors which could materially affect the Group's future results are set out on pages 268 to 293. The Group's regulatory capital resources and significant developments in 2014 and anticipated future developments are detailed on pages 40 to 49. The liquidity and funding section on pages 50 to 58 describes the Group's funding and liquidity profile, including changes in key metrics and the build up of liquidity reserves.

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

Corporate governance

Internal control over financial reporting

The internal controls over financial reporting for the Group are consistent with those at the RBS Group level. The RBS Group is required to comply with Section 404 of the US Sarbanes-Oxley Act of 2002 and assess the effectiveness of internal control over financial reporting as of 31 December 2015.

The RBS Group has assessed the effectiveness of its internal control over financial reporting as of 31 December 2015 based on the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in the 2013 publication of 'Internal Control - Integrated Framework'.

Based on its assessment, management has concluded that, as of 31 December 2015, RBS Group's internal control over financial reporting is effective.

The RBS Group's auditors have audited the effectiveness of the RBS Group's internal control over financial reporting and have given an unqualified opinion.

Management's report on RBS Group's internal control over financial reporting was filed with the Securities and Exchange Commission as part of the 2015 Annual Report on Form 20-F.

Board of directors

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

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

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

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

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

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

The Group Performance and Remuneration Committee comprises at least three independent non-executive directors and has oversight of the Group's policy on remuneration. It also considers senior executive remuneration and makes recommendations to the Board on remuneration of executive directors.

The Group Nominations and Governance Committee comprises all of the non-executive directors. It assists the Board in the selection and appointment of directors. It reviews the structure, size and composition of the Board, and membership and chairmanship of Board committees.

The Sustainable Banking Committee comprises of independent non-executive directors and is chaired by the Senior Independent Director. It is responsible for overseeing and challenging how management is addressing sustainability and reputation issues relating to all stakeholder groups, except where such issues have already been dealt with by other Board committees.

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

Share capital

Details of the ordinary and preference share capital at 31 December 2015 are shown in Note 24 on the accounts.

Directors

The current members of the Board are shown on page 2.

Sandy Crombie, Alison Davis, Morten Friis, Robert Gillespie, Penny Hughes, Ross McEwan, Brendan Nelson, Baroness Noakes and Ewen Stevenson all served throughout the year and to the date of signing of the financial statements.

Howard Davies was appointed to the Board on 14 July 2015 and assumed the role of Chairman on 1 September 2015. Mike Rogers was appointed to the Board on 26 January 2016.

Philip Hampton stepped down from the Board on 31 August 2015.

All directors of the company are required to stand for election or re-election annually by shareholders at the Annual General Meeting.

Directors' interests

The interests of the directors in the shares of the holding company at 31 December 2015 are disclosed in the Report and Accounts of that company. None of the directors held an interest in the loan capital of the holding company or in the shares or loan capital of the Bank or any of the subsidiaries of the Bank, during the period from 1 January 2015 to 30 March 2016

Directors' indemnities

In terms of section 236 of the Companies Act 2006 (the "Companies Act"), Qualifying Third Party Indemnity Provisions have been issued by the holding company to directors, members of the Group's Executive and Management Committees, PRA/FCA Approved Persons and certain directors and/or officers of the Group's subsidiaries.

In terms of section 236 of the Companies Act, Qualifying Pension Scheme Indemnity Provisions have been issued to all trustees of the Group's pension schemes.

Post balance sheet events

Other than the matters disclosed in Note 40 on the accounts, there have been no significant events between the year end and the date of approval of these accounts which would require a change to or additional disclosure in the accounts.

Political donations

During 2015, no political donations were made in the UK or EU, nor any political expenditure incurred in the UK or EU.

Directors' disclosure to auditors

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

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

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

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act.

Auditors

Deloitte LLP are currently the auditors. On 3 November 2014, the Company announced its intention to appoint Ernst & Young LLP (EY) as auditor for the year ending 31 December 2016. It is expected that EY will be appointed to fill the casual vacancy arising from Deloitte LLP's resignation following the signing of the Group's 2015 accounts. A resolution to appoint EY as the company's auditors will be proposed at the forthcoming Annual General Meeting.

By order of the Board

Aileen Taylor
Company Secretary
30 March 2016

The Royal Bank of Scotland plc
is registered in Scotland No. SC90312.

Statement of directors' responsibilities

This statement should be read in conjunction with the responsibilities of the auditor set out in their report on pages 141.

The directors are responsible for the preparation of the Annual Report and Accounts. The directors are required by Article 4 of the IAS Regulation (European Commission Regulation No 1606/2002) to prepare Group accounts, and as permitted by the Companies Act 2006 have elected to prepare Bank accounts, for each financial year in accordance with International Financial Reporting Standards as adopted by the European Union. They are responsible for preparing accounts that present fairly the financial position, financial performance and cash flows of the Group and the Bank. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the Annual Report and Accounts complies with the Companies Act 2006. 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.

The directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with International Financial Reporting Standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Bank and the undertakings included in the consolidation taken as a whole; and
- the Strategic report and Director's report (incorporating the Financial review) includes a fair review of the development and performance of the business and the position of the Bank and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

Howard Davies Chairman	Ross McEwan Chief Executive	Ewen Stevenson Chief Financial Officer

30 March 2016

Board of directors

Chairman
Howard Davies

Executive directors
Ross McEwan
Ewen Stevenson

Non-executive directors
Sandy Crombie
Alison Davis
Morten Friis
Robert Gillespie
Penny Hughes
Brendan Nelson
Baroness Noakes
Mike Rogers

Financial statements

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Independent auditor's report to the members of The Royal Bank of Scotland plc

We have audited the financial statements of The Royal Bank of Scotland plc ("the Bank") and its subsidiaries (together the "Group") for the year ended 31 December 2015 which comprise the accounting policies, the balance sheets as at 31 December 2015, the consolidated income statement, the consolidated statement of comprehensive income, the statements of changes in equity and the cash flow statements for the year ended 31 December 2015, the related notes 1 to 41 and the information identified as 'audited' in the Capital and risk management section of the Financial review. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union and, as regards the Bank financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Bank's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the statement of directors' responsibilities the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Bank's affairs as at 31 December 2015 and of the Group's loss for the year then ended;
- the Group's financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation; and
- the Bank's financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006.

Separate opinion in relation to IFRSs as issued by the IASB

As explained in the accounting policies, the Group in addition to complying with its legal obligation to apply IFRSs as adopted by the European Union, has also applied IFRSs as issued by the International Accounting Standards Board (IASB).

In our opinion the Group financial statements comply with IFRSs as issued by the IASB.

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

- adequate accounting records have not been kept by the Bank, or returns adequate for our audit have not been received from branches not visited by us; or
- the Bank financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Michael Lloyd (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
30 March 2016

Consolidated income statement for the year ended 31 December 2015

	Note	2015 £m	2014 £m	2013 £m
Interest receivable		11,746	12,805	14,151
Interest payable		(3,338)	(3,939)	(5,521)
Net interest income	1	8,408	8,866	8,630
Fees and commissions receivable		3,692	4,320	4,598
Fees and commissions payable		(805)	(842)	(892)
Income from trading activities		954	1,190	2,860
(Loss)/gain on redemption of own debt		(263)	6	162
Other operating income		165	1,078	1,397
Non-interest income	2	3,743	5,752	8,125
Total income		12,151	14,618	16,755
Staff costs		(5,668)	(5,683)	(5,929)
Premises and equipment		(1,809)	(2,059)	(1,994)
Other administrative expenses		(6,160)	(4,361)	(6,530)
Depreciation and amortisation		(1,173)	(926)	(1,109)
Write down of goodwill and other intangible assets		(1,331)	(523)	(423)
Operating expenses	3	(16,141)	(13,552)	(15,985)
(Loss)/profit before impairment releases/(losses)		(3,990)	1,066	770
Impairment releases/(losses)	11	837	1,337	(8,137)
Operating (loss)/profit before tax		(3,153)	2,403	(7,367)
Tax credit/(charge)	6	29	(2,033)	(307)
(Loss)/profit from continuing operations		(3,124)	370	(7,674)
Profit/(loss) from discontinued operations, net of tax		1,538	(3,486)	410
Loss for the year		(1,586)	(3,116)	(7,264)
Attributable to:				
Non-controlling interests		320	57	(13)
Preference shareholders		44	61	58
Ordinary shareholders		(1,950)	(3,234)	(7,309)
		(1,586)	(3,116)	(7,264)

The accompanying notes on pages 163 to 264, the accounting policies on pages 148 to 162 and the audited sections of the Financial review: Capital and risk management on pages 28 to 134 form an integral part of these financial statements.

Consolidated statement of comprehensive income for the year ended 31 December 2015

	Note	2015 £m	2014* £m	2013* £m
Loss for the year		(1,586)	(3,116)	(7,264)
Items that do not qualify for reclassification				
(Loss)/gain on remeasurement of retirement benefit schemes	4	(73)	(1,849)	389
Tax		306	314	(237)
		233	(1,535)	152
Items that do qualify for reclassification				
Available-for-sale financial assets		13	132	(1,907)
Cash flow hedges		(740)	1,412	(2,485)
Currency translation		(1,123)	434	(197)
Tax		136	(401)	1,101
		(1,714)	1,577	(3,488)
Other comprehensive (loss)/income after tax		(1,481)	42	(3,336)
Total comprehensive loss for the year		(3,067)	(3,074)	(10,600)
Attributable to:				
Non-controlling interests		315	194	(10)
Preference shareholders		44	61	58
Ordinary shareholders		(3,426)	(3,329)	(10,648)
		(3,067)	(3,074)	(10,600)

*Restated - refer to page 148 for further details

Note:
(1) A profit of £1,220 million (2014 - loss £3,538 million; 2013 - profit £410 million) from discontinued operations was attributable to ordinary shareholders.

The accompanying notes on pages 163 to 264, the accounting policies on pages 148 to 162 and the audited sections of the Financial review: Capital and risk management on pages 28 to 134 form an integral part of these financial statements.

Balance sheet as at 31 December 2015

	Note	Group 2015 £m	Group 2014* £m	Bank 2015 £m	Bank 2014 £m
Assets					
Cash and balances at central banks	8	78,999	73,983	76,904	70,952
Amounts due from subsidiaries	8	1,557	2,333	24,091	24,839
Other loans and advances to banks	8	28,285	42,259	21,259	30,062
Loans and advances to banks	8	29,842	44,592	45,350	54,901
Amounts due from holding company and subsidiaries	8	1,258	1,323	28,283	41,196
Other loans and advances to customers	8	333,699	375,615	133,369	176,581
Loans and advances to customers	8	334,957	376,938	161,652	217,777
Debt securities subject to repurchase agreements	27	20,224	22,923	16,484	14,332
Other debt securities		59,803	61,351	60,118	73,262
Debt securities	13	80,027	84,274	76,602	87,594
Equity shares	14	1,069	5,203	931	4,880
Investments in Group undertakings	15	—	—	34,482	39,857
Settlement balances		4,108	4,710	3,053	3,381
Amounts due from holding company and subsidiaries	12	1,275	2,738	4,726	9,268
Other derivatives	12	261,808	351,844	260,875	350,557
Derivatives	12	263,083	354,582	265,601	359,825
Intangible assets	16	6,526	7,765	544	917
Property, plant and equipment	17	4,453	6,123	1,612	1,976
Deferred tax	22	2,622	1,881	902	733
Prepayments, accrued income and other assets	18	3,019	4,298	1,549	2,203
Assets of disposal groups	19	3,486	81,033	—	—
Total assets		812,191	1,045,382	669,182	844,996
Liabilities					
Amounts due to subsidiaries	8	3,999	4,208	116,343	121,489
Other deposits by banks	8	38,095	59,642	30,877	52,966
Deposits by banks	8	42,094	63,850	147,220	174,455
Amounts due to holding company and subsidiaries	8	5,021	5,843	16,867	29,240
Other customers accounts	8	369,053	389,156	121,907	144,276
Customer accounts	8	374,074	394,999	138,774	173,516
Debt securities in issue	8	25,804	41,996	23,361	36,743
Settlement balances		3,383	4,498	2,363	3,098
Short positions	20	20,808	23,028	17,593	16,590
Amounts due to holding company and subsidiaries	12	1,283	2,005	3,528	6,585
Other derivatives	12	254,265	348,778	253,844	348,162
Derivatives	12	255,548	350,783	257,372	354,747
Provisions, accruals and other liabilities	21	14,070	12,262	5,676	5,622
Retirement benefit liabilities	4	3,764	4,289	112	192
Deferred tax	22	729	236	—	—
Amounts due to holding company	8	18,502	19,639	18,485	18,535
Other subordinated liabilities	8	8,528	10,830	7,049	8,945
Subordinated liabilities	23	27,030	30,469	25,534	27,480
Liabilities of disposal groups	19	2,980	71,284	—	—
Total liabilities		770,284	997,694	618,005	792,443
Non-controlling interests		54	2,385	—	—
Owners' equity	24	41,853	45,303	51,177	52,553
Total equity		41,907	47,688	51,177	52,553
Total liabilities and equity		812,191	1,045,382	669,182	844,996

*Restated - refer to page 148 for further details.

The accompanying notes on pages 163 to 264, the accounting policies on pages 148 to 162 and the audited sections of the Financial review: Capital and risk management on pages 28 to 134 form an integral part of these financial statements.

The accounts were approved by the Board of directors on 30 March 2016 and signed on its behalf by:

Howard Davies	Ross McEwan	Ewen Stevenson
Chairman	Chief Executive	Chief Financial Officer

The Royal Bank of Scotland plc
Registration No. SC90312

Statement of changes in equity for the year ended 31 December 2015

	Group			Bank		
	2015 £m	2014* £m	2013* £m	2015 £m	2014 £m	2013 £m
Called-up share capital						
At 1 January and 31 December	6,609	6,609	6,609	6,609	6,609	6,609
Share premium account						
At 1 January	26,807	26,290	26,081	26,807	26,290	26,081
Redemption of preference shares classified as debt	—	517	—	—	517	—
Ordinary share issued on cross-border merger (1)	—	—	209	—	—	209
At 31 December	26,807	26,807	26,290	26,807	26,807	26,290
Merger reserve						
At 1 January	10,834	10,800	10,881	(47)	(81)	—
Unwind of merger reserve	31	34	—	31	34	—
Merger reserve created on cross-border merger (1)	—	—	(81)	—	—	(81)
At 31 December	10,865	10,834	10,800	(16)	(47)	(81)
Available-for-sale reserve						
At 1 January	400	359	1,750	252	302	1,443
Unrealised gains/(losses)	88	504	(844)	121	261	(558)
Realised gains	(70)	(409)	(1,063)	(44)	(323)	(939)
Tax	(18)	(45)	516	(32)	12	356
Recycled to profit or loss on ceding control of Citizens (2)	9	—	—	—	—	—
Transfer to retained earnings	(43)	(9)	—	—	—	—
At 31 December	366	400	359	297	252	302
Cash flow hedging reserve						
At 1 January	1,026	(86)	1,815	755	350	1,767
Amount recognised in equity	668	2,869	(1,082)	398	1,625	(566)
Amount transferred from equity to earnings	(1,350)	(1,457)	(1,403)	(944)	(1,119)	(1,291)
Tax	106	(334)	584	77	(101)	440
Recycled to profit or loss on ceding control of Citizens (3)	(36)	—	—	—	—	—
Transfer to retained earnings	9	34	—	—	—	—
At 31 December	423	1,026	(86)	286	755	350
Foreign exchange reserve						
At 1 January	1,762	1,842	2,041	(246)	(357)	(291)
Retranslation of net assets	(79)	403	(287)	30	110	(66)
Foreign currency (losses)/gains on hedges of net assets	(74)	(82)	87	24	1	—
Tax	11	(9)	1	—	—	—
Recycled to profit or loss on disposal of businesses	4	—	—	—	—	—
Recycled to profit or loss on ceding of control Citizens	(974)	—	—	—	—	—
Transfer to retained earnings	(642)	(392)	—	—	—	—
At 31 December	8	1,762	1,842	(192)	(246)	(357)

*Restated - refer to page 148 for further details.

For notes to these tables refer to page 146.

Statement of changes in equity for the year ended 31 December 2015

	Group			Bank		
	2015 £m	2014* £m	2013* £m	2015 £m	2014 £m	2013 £m
Retained earnings						
At 1 January	(2,135)	2,888	10,072	18,423	21,209	22,501
(Loss)/profit attributable to ordinary and equity preference shareholders						
- continuing operations	(3,126)	365	(7,661)	(1,031)	(2,058)	(1,199)
- discontinued operations	1,220	(3,538)	410	—	—	—
Equity preference dividends paid	(44)	(61)	(58)	(44)	(61)	(58)
Transfer from available-for-sale reserve	43	9	—	—	—	—
Transfer from cash flow hedging reserve	(9)	(34)	—	—	—	—
Transfer from foreign exchange reserve	642	392	—	—	—	—
Costs of placing Citizens equity	(29)	(45)	—	—	—	—
(Loss)/gain on remeasurement of retirement benefit schemes (4)						
- gross	(67)	(1,849)	389	84	(107)	(13)
- tax	306	314	(237)	(20)	16	6
Redemption of preference shares classified as debt	—	(517)	—	—	(517)	—
Shares issued under employee share schemes	(58)	(91)	(76)	(58)	(91)	(76)
Share-based payments						
- gross	36	29	48	36	29	48
- tax	(4)	3	1	(4)	3	—
At 31 December	(3,225)	(2,135)	2,888	17,386	18,423	21,209
Owners' equity at 31 December	41,853	45,303	48,702	51,177	52,553	54,322
Non-controlling interests						
At 1 January	2,385	79	137	—	—	—
Currency translation adjustments and other movements	28	113	3	—	—	—
- continuing operations	2	5	(13)	—	—	—
- discontinued operations	318	52	—	—	—	—
Dividends paid	(31)	(4)	(5)	—	—	—
Movements in available-for-sale securities						
- unrealised gains	25	37	—	—	—	—
- tax	(5)	(13)	—	—	—	—
Movements in cash flow hedging reserve						
- amount recognised in equity	32	18	—	—	—	—
- recycled to profit or loss on disposal of discontinued operations	—	(18)	—	—	—	—
- tax	(4)	—	—	—	—	—
Actuarial losses recognised in retirement benefit schemes	(6)	—	—	—	—	—
Equity raised (5)	2,491	2,117	—	—	—	—
Equity withdrawn and disposals	(24)	(1)	(43)	—	—	—
Loss of control of Citizens	(5,157)	—	—	—	—	—
At 31 December	54	2,385	79	—	—	—
Total equity at 31 December	41,907	47,688	48,781	51,177	52,553	54,322
Total equity is attributable to:						
Non-controlling interests	54	2,385	79	—	—	—
Preference shareholders	1,421	1,421	1,421	1,421	1,421	1,421
Ordinary shareholders	40,432	43,882	47,281	49,756	51,132	52,901
	41,907	47,688	48,781	51,177	52,553	54,322

*Restated - refer to page 148 for further details.

Notes:
(1) See Note 24.
(2) Net of tax - £6 million charge.
(3) Net of tax - £16 million credit.
(4) See change of accounting policy on page 148.
(5) Includes £2,491 million relating to the secondary offering of Citizens in March 2015 (2014 - £2,117 million relating to the IPO of Citizens).

The accompanying notes on pages 163 to 264, the accounting policies on pages 148 to 162 and the audited sections of the Financial review: Capital and risk management on pages 28 to 134 form an integral part of these financial statements.

Cash flow statement for the year ended 31 December 2015

	Note	Group 2015 £m	Group 2014* £m	Group 2013* £m	Bank 2015 £m	Bank 2014 £m	Bank 2013 £m
Cash flows from operating activities							
Operating (loss)/profit before tax from continuing operations		(3,153)	2,403	(7,367)	(1,451)	(959)	8
Profit/(loss) before tax from discontinued operations		1,750	(3,258)	606	—	—	—
Adjustments for non-cash items and other adjustments included within income statement		(6,972)	(283)	5,757	6,171	3,477	272
Cash contribution to defined benefit pension schemes		(1,059)	(1,063)	(817)	(32)	(28)	(41)
Changes in operating assets and liabilities		10,787	(11,917)	(18,949)	992	(30,276)	(22,151)
Income taxes (paid)/received		(231)	(302)	(195)	(192)	135	322
Net cash flows from operating activities	30	1,122	(14,420)	(20,965)	5,488	(27,651)	(21,590)
Cash flows from investing activities							
Sale and maturity of securities		6,345	17,631	33,741	17,877	22,926	33,660
Purchase of securities		(12,882)	(19,945)	(21,667)	(11,451)	(12,022)	(14,310)
Sale of property, plant and equipment		1,541	1,161	888	305	164	83
Purchase of property, plant and equipment		(761)	(810)	(697)	(338)	(273)	(321)
Net divestment of/(investment in) business interests and intangible assets	31	53	(2,947)	4,237	(3,937)	(2,358)	1,646
Net cash flows from investing activities		(5,704)	(4,910)	16,502	2,456	8,437	20,758
Cash flows from financing activities							
Issue of subordinated liabilities		—	1,438	2,285	—	833	1,864
Proceeds of non-controlling interests issued		2,491	2,117	—	—	—	—
Redemption of non-controlling interests		—	(1)	(43)	—	—	—
Repayment of subordinated liabilities		(2,279)	(4,181)	(1,868)	(1,894)	(4,121)	(1,868)
Dividends paid		(75)	(65)	(63)	(44)	(61)	(58)
Interest on subordinated liabilities		(1,313)	(1,308)	(1,395)	(1,338)	(1,236)	(1,325)
Net cash flows from financing activities		(1,176)	(2,000)	(1,084)	(3,276)	(4,585)	(1,387)
Effects of exchange rate changes on cash and cash equivalents		525	682	402	575	541	604
Net (decrease)/increase in cash and cash equivalents		(5,233)	(20,648)	(5,145)	5,243	(23,258)	(1,615)
Cash and cash equivalents at 1 January		107,308	127,956	133,101	101,370	124,628	126,243
Cash and cash equivalents at 31 December	34	102,075	107,308	127,956	106,613	101,370	124,628

*Restated - refer to page 148 for further details.

The accompanying notes on pages 163 to 264, the accounting policies on pages 148 to 162 and the audited sections of the Financial review: Capital and risk management on pages 28 to 134 form an integral part of these financial statements.

Accounting policies

1.Presentation of accounts

The accounts are prepared on a going concern basis (see the Report of the directors, page 137) and in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board (IASB) and interpretations issued by the IFRS Interpretations Committee of the IASB as adopted by the European Union (EU) (together IFRS). The EU has not adopted the complete text of IAS 39 'Financial Instruments: Recognition and Measurement'; it has relaxed some of the standard's hedging requirements. The Group has not taken advantage of this relaxation: its financial statements are prepared in accordance with IFRS as issued by the IASB.

The company is incorporated in the UK and registered in Scotland. Its accounts are presented in accordance with the Companies Act 2006. With the exception of investment property and certain financial instruments as described in Accounting policies 9, 14, 16 and 18, the accounts are presented on a historical cost basis.

On 31 December 2014, Citizens Financial Group Inc. was classified as a discontinued operation and a disposal group: its aggregate assets were presented in Assets of disposal groups and its aggregate liabilities in Liabilities of disposal groups. Prior period results were re-presented.

From 3 August 2015, when the Group's interest in Citizens fell to 20.9%, Citizens was accounted for as an associate classified as held for sale. The Group subsequently completed its divestment of Citizens when it sold its final tranche on 30 October 2015. Citizens is no longer a reportable segment, therefore segment disclosures for all periods have been restated.

Change of accounting policy

The Group changed its accounting policy for the recognition of surpluses in its defined benefit pension schemes: in particular, the policy for determining whether or not it has an unconditional right to a refund of surpluses in its employee pension funds. Where the Group has a right to a refund, this is not deemed unconditional if pension fund trustees are able unilaterally to enhance benefits for plan members. As a result of this change, a minimum funding requirement to cover an existing shortfall in a scheme may give rise to an additional liability and surpluses may not be recognised in full. The revised accounting policy, by taking account of the powers of pension trustees in assessing the economic benefit available as a refund, provides more relevant information about the effect on the Group's financial position of its defined benefit pension schemes.

In accordance with IFRS, the amended policy has been applied retrospectively and prior periods restated. The impact of the change in policy is set out below.

Consolidated income statement

	2015		
	Under previous policy £m	Adjustment £m	As published £m
Staff costs	(5,604)	(64)	(5,668)
Operating expenses	(16,077)	(64)	(16,141)
Loss before impairment losses	(3,926)	(64)	(3,990)
Operating loss before tax	(3,089)	(64)	(3,153)
Tax charge	17	12	29
Loss from continuing operations	(3,072)	(52)	(3,124)
Loss for the year	(1,534)	(52)	(1,586)
Loss attributable to ordinary shareholders	(1,898)	(52)	(1,950)

There are no adjustments to the income statement in 2014 and 2013.

Consolidated statement of comprehensive income

	2015			2014			2013		
	Under previous policy £m	Adjustment £m	As published £m	As previously reported £m	Adjustment £m	Restated £m	As previously reported £m	Adjustment £m	Restated £m
Loss for the year	(1,534)	(52)	(1,586)	(3,116)	—	(3,116)	(7,264)	—	(7,264)
Gain/(loss) on remeasurement of retirement benefit schemes	1,139	(1,212)	(73)	(100)	(1,749)	(1,849)	443	(54)	389
Tax	(147)	453	306	(36)	350	314	(246)	9	(237)
Total comprehensive loss after tax	(2,256)	(811)	(3,067)	(1,675)	(1,399)	(3,074)	(10,555)	(45)	(10,600)

Consolidated balance sheet

	2015			2014			2013		
	Under previous policy £m	Adjustment £m	As published £m	As previously reported £m	Adjustment £m	Restated £m	As previously reported £m	Adjustment £m	Restated £m
Deferred tax assets	1,786	836	2,622	1,510	371	1,881	3,435	21	3,456
Prepayments, accrued income and other assets	3,168	(149)	3,019	4,413	(115)	4,298	5,904	(77)	5,827
Retirement benefit liabilities	783	2,981	3,764	2,550	1,739	4,289	3,188	28	3,216
Owners' equity	44,147	(2,294)	41,853	46,786	(1,483)	45,303	48,786	(84)	48,702

Consolidated statement of changes in equity

	2015			2014			2013		
	Under previous policy £m	Adjustment £m	As published £m	As previously reported £m	Adjustment £m	Restated £m	As previously reported £m	Adjustment £m	Restated £m
Retained earnings									
At 1 January	(652)	(1,483)	(2,135)	2,972	(84)	2,888	10,111	(39)	10,072
(Loss)/profit attributable to ordinary shareholders and other equity owners - continuing operations	(3,074)	(52)	(3,126)	365	—	365	(7,661)	—	(7,661)
Gain/(loss) on remeasurement of retirement benefit schemes									
- gross	1,145	(1,212)	(67)	(100)	(1,749)	(1,849)	443	(54)	389
- tax	(147)	453	306	(36)	350	314	(246)	9	(237)
At 31 December	(931)	(2,294)	(3,225)	(652)	(1,483)	(2,135)	2,972	(84)	2,888

The Group adopted a number of new and revised IFRSs effective 1 January 2015:

IAS 19 'Defined Benefit Plans: Employee Contributions' was issued in November 2013. This amendment distinguishes the accounting for employee contributions that are related to service from those that are independent of service.

Annual Improvements to IFRS 2010 - 2012 and 2011 - 2013 cycles were issued in December 2013 making a number of minor amendments to IFRS.

The implementation of these requirements has not had a material effect on the Group's accounts.

2. Basis of consolidation

The consolidated accounts incorporate the financial statements of the company and entities (including certain structured entities) that are controlled by the Group. The Group controls another entity (a subsidiary) when it is exposed, or has rights, to variable returns from its involvement with that entity and has the ability to affect those returns through its power over the other entity; power generally arises from holding a majority of voting rights. On acquisition of a subsidiary, its identifiable assets, liabilities and contingent liabilities are included in the consolidated accounts at their fair value. A subsidiary is consolidated financial statements from the date it is controlled by the Group until the date the Group ceases to control it through a sale or a significant change in circumstances. Changes in the Group's interest in a subsidiary that do not result in the Group ceasing to control that subsidiary are accounted for as equity transactions.

All intergroup balances, transactions, income and expenses are eliminated on consolidation. The consolidated accounts are prepared under uniform accounting policies.

3. Revenue recognition

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

Financial assets and financial liabilities held for trading or designated as at fair value through profit or loss are recorded at fair value. Changes in fair value are recognised in profit or loss.

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

The application of this policy to significant fee types is outlined below.

Payment services - this comprises income received for payment services including cheques cashed, direct debits, Clearing House Automated Payments (the UK electronic settlement system) and BACS payments (the automated clearing house that processes direct debits and direct credits). These are generally charged on a per transaction basis. The income is earned when the payment or transaction occurs. Charges for payment services are usually debited to the customer's account monthly or quarterly in arrears. Income is accrued at period end for services provided but not yet charged.

Credit and debit card fees - fees from card business include:

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

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

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

Trade finance – income from the provision of trade finance is recognised over the term of the finance unless specifically related to a significant act, in which case income is recognised when the act is executed.

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

4. Assets held for sale and discontinued operations

A non-current asset (or disposal group) is classified as held for sale if the Group will recover its carrying amount principally through a sale transaction rather than through continuing use. A non-current asset (or disposal group) classified as held for sale is measured at the lower of its carrying amount and fair value less costs to sell. If the asset (or disposal group) is acquired as part of a business combination it is initially measured at fair value less costs to sell. Assets and liabilities of disposal groups classified as held for sale and non-current assets classified as held for sale are shown separately on the face of the balance sheet.

The results of discontinued operations - comprising the post-tax profit or loss of discontinued operations and the post-tax gain or loss recognised either on measurement to fair value less costs to sell or on disposal of the discontinued operation - are shown as a single amount on the face of the income statement; an analysis of this amount is presented in Note 19 on the accounts. A discontinued operation is a cash generating unit or a group of cash generating units that either has been disposed of, or is classified as held for sale, and (a) represents a separate major line of business or geographical area of operations, (b) is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations or (c) is a subsidiary acquired exclusively with a view to resale.

5. Employee benefits

Short-term employee benefits, such as salaries, paid absences, and other benefits are accounted for on an accruals basis over the period in which the employees provide the related services. Employees may receive variable compensation satisfied by cash, by debt instruments issued by the Group or by RBSG shares. The treatment of share-based compensation is set out in Accounting policy 24. Variable compensation that is settled in cash or debt instruments is charged to profit or loss over the period from the start of the year to which the variable compensation relates to the expected settlement date taking account of forfeiture and claw back criteria.

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

Contributions to defined contribution pension schemes are recognised in profit or loss when payable.

For defined benefit schemes, the defined benefit obligation is measured on an actuarial basis using the projected unit credit method and discounted at a rate determined by reference to market yields at the end of the reporting period on high quality corporate bonds of equivalent term and currency to the scheme liabilities. Scheme assets are measured at their fair value. The difference between scheme assets and scheme liabilities – the net defined benefit asset or liability - is recognised in the balance sheet. A defined benefit asset is limited to the present value of any economic benefits available to the Group in the form of refunds from the plan or reduced contributions to it.

The charge to profit or loss for pension costs (recorded in operating expenses) comprises:

- the current service cost
- interest, computed at the rate used to discount scheme liabilities, on the net defined benefit liability or asset
- past service cost resulting from a scheme amendment or curtailment
- gains or losses on settlement.

A curtailment occurs when the Group significantly reduces the number of employees covered by a plan. A plan amendment occurs when the Group introduces, or withdraws, a defined benefit plan or changes the benefits payable under an existing defined benefit plan. Past service cost may be either positive (when benefits are introduced or changed so that the present value of the defined benefit obligation increases) or negative (when benefits are withdrawn or changed so that the present value of the defined benefit obligation decreases). A settlement is a transaction that eliminates all further obligation for part or all of the benefits.

Actuarial gains and losses (i.e. gains or and losses on re-measuring the net defined benefit asset or liability) are recognised in other comprehensive income in full in the period in which they arise.

6. Intangible assets and goodwill

Intangible assets acquired by the Group are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to profit or loss over the assets' estimated economic lives using methods that best reflect the pattern of economic benefits and is included in Depreciation and amortisation. These estimated useful economic lives are:

Computer software	3 to 12 years
Other acquired intangibles	5 to 10 years

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

Intangible assets include goodwill arising on the acquisition of subsidiaries and joint ventures. Goodwill on the acquisition of a subsidiary is the excess of the fair value of the consideration transferred, the fair value of any existing interest in the subsidiary and the amount of any non-controlling interest measured either at fair value or at its share of the subsidiary’s net assets over the Group's interest in the net fair value of the subsidiary’s identifiable assets, liabilities and contingent liabilities. Goodwill arises on the acquisition of a joint venture when the cost of investment exceeds the Group’s share of the net fair value of the joint venture’s identifiable assets and liabilities. Goodwill is measured at initial cost less any subsequent impairment losses. Goodwill arising on the acquisition of associates is included within their carrying amounts. The gain or loss on the disposal of a subsidiary, associate or joint venture includes the carrying value of any related goodwill.

7. Property, plant and equipment

Items of property, plant and equipment (except investment property - see Accounting policy 9) are stated at cost less accumulated depreciation and impairment losses. Where an item of property, plant and equipment comprises major components having different useful lives, these are accounted for separately.

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

The estimated useful lives of the Group's property, plant and equipment are:

Freehold buildings	50 years
Long leasehold property (leases with more than 50 years to run)	50 years
Short leaseholds	unexpired period of the lease
Property adaptation costs	10 to 15 years
Computer equipment	up to 5 years
Other equipment	4 to 15 years

The residual value and useful life of property, plant and equipment are reviewed at each balance sheet date and updated for any changes to previous estimates.

8. Impairment of intangible assets and property, plant and equipment

At each reporting date, the Group assesses whether there is any indication that its intangible assets, or property, plant and equipment are impaired. If any such indication exists, the Group estimates the recoverable amount of the asset and the impairment loss if any. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired.

If an asset does not generate cash flows that are independent from those of other assets or groups of assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. For the purposes of impairment testing, goodwill acquired in a business combination is allocated to each of the Group's cash-generating units or groups of cash-generating units expected to benefit from the combination. The recoverable amount of an asset or cash-generating unit is the higher of its fair value less cost to sell and its value in use. Value in use is the present value of future cash flows from the asset or cash-generating unit discounted at a rate that reflects market interest rates adjusted for risks specific to the asset or cash-generating unit that have not been taken into account in estimating future cash flows. If the recoverable amount of an intangible or tangible asset is less than its carrying value, an impairment loss is recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss.

A reversal of an impairment loss on intangible assets (excluding goodwill) or property, plant and equipment is recognised as it arises provided the increased carrying value is not greater than it would have been had no impairment loss been recognised. Impairment losses on goodwill are not reversed.

9. Investment property

Investment property comprises freehold and leasehold properties that are held to earn rentals or for capital appreciation or both. Investment property is not depreciated but is stated at fair value. Fair value is based on current prices for similar properties in the same location and condition. Any gain or loss arising from a change in fair value is recognised in profit or loss.
Rental income from investment property is recognised on a straight-line basis over the term of the lease in Other operating income. Lease incentives granted are recognised as an integral part of the total rental income.

10. Foreign currencies

The Group's consolidated financial statements are presented in sterling which is the functional currency of the company.

Group entities record transactions in foreign currencies in their functional currency - the currency of the primary economic environment in which they operate - at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the relevant functional currency at the foreign exchange rates ruling at the balance sheet date. Foreign exchange differences arising on the settlement of foreign currency transactions and from the translation of monetary assets and liabilities are reported in income from trading activities except for differences arising on cash flow hedges and hedges of net investments in foreign operations (see Accounting policy 23).

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

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

11. Leases

As Lessor

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

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

Rental income from operating leases is recognised in income on a straight-line basis over the lease term unless another systematic basis better represents the time pattern of the asset's use. Operating lease assets are included within Property, plant and equipment and depreciated over their useful lives (see Accounting policy 7). Operating lease rentals receivable are included in Other operating income.

As lessee

The Group's contracts to lease assets are principally operating leases. Operating lease rental expense is included in Premises and equipment costs and recognised as an expense on a straight-line basis over the lease term unless another systematic basis better represents the benefit to the Group.

12. Provisions

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

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

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

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

13. Tax

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

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

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

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

14. Financial assets

On initial recognition, financial assets are classified into held-to-maturity investments; held-for-trading; designated as at fair value through profit or loss; loans and receivables; or available-for-sale financial assets. Regular way purchases of financial assets classified as loans and receivables are recognised on settlement date; all other regular way transactions in financial assets are recognised on trade date.

Held-to-maturity investments - a financial asset may be classified as a held-to-maturity investment only if it has fixed or determinable payments, a fixed maturity and the Group has the positive intention and ability to hold to maturity. Held-to-maturity investments are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at amortised cost using the effective interest method (see Accounting policy 3) less any impairment losses.

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

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

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

Loans and receivables - non-derivative financial assets with fixed or determinable repayments that are not quoted in an active market are classified as loans and receivables, except those that are classified as available-for-sale or as held-for-trading, or designated as at fair value through profit or loss. Loans and receivables are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at amortised cost using the effective interest method (see Accounting policy 3) less any impairment losses.

Available-for-sale financial assets - financial assets that are not classified as held-to-maturity; held-for-trading; designated as at fair value through profit or loss; or loans and receivables are classified as available-for-sale. Financial assets can be designated as available-for-sale on initial recognition. Available-for-sale financial assets are initially recognised at fair value plus directly related transaction costs.

They are subsequently measured at fair value. Unquoted equity investments whose fair value cannot be measured reliably are carried at cost and classified as available-for-sale financial assets. Impairment losses and exchange differences resulting from retranslating the amortised cost of foreign currency monetary available-for-sale financial assets are recognised in profit or loss together with interest calculated using the effective interest method (see Accounting policy 3) as are gains and losses attributable to the hedged risk on available-for-sale financial assets that are hedged items in fair value hedges (see Accounting policy 23). Other changes in the fair value of available-for-sale financial assets and any related tax are reported in other comprehensive income until disposal, when the cumulative gain or loss is reclassified from equity to profit or loss.

Reclassifications - held-for-trading and available-for-sale financial assets that meet the definition of loans and receivables (non-derivative financial assets with fixed or determinable payments that are not quoted in an active market) may be reclassified to loans and receivables if the Group has the intention and ability to hold the financial asset for the foreseeable future or until maturity. The Group typically regards the foreseeable future for this purpose as twelve months from the date of reclassification. Additionally, held-for-trading financial assets that do not meet the definition of loans and receivables may, in rare circumstances, be transferred to available-for-sale financial assets or to held-to-maturity investments. Reclassifications are made at fair value. This fair value becomes the asset's new cost or amortised cost as appropriate. Gains and losses recognised up to the date of reclassification are not reversed.

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

15. Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or group of financial assets classified as held-to-maturity, as available-for-sale or as loans and receivables is impaired. A financial asset or group of financial assets is impaired and an impairment loss incurred if there is objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset.

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

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

Impairment losses are assessed individually for financial assets that are individually significant and individually or collectively for assets that are not individually significant. In making collective impairment assessments, financial assets are grouped into portfolios on the basis of similar risk characteristics. Future cash flows from these portfolios are estimated on the basis of the contractual cash flows and historical loss experience for assets with similar credit risk characteristics.

Historical loss experience is adjusted, on the basis of observable data, to reflect current conditions not affecting the period of historical experience. Impairment losses are recognised in profit or loss and the carrying amount of the financial asset or group of financial assets reduced by establishing an allowance for impairment losses. If, in a subsequent period, the amount of the impairment loss reduces and the reduction can be ascribed to an event after the impairment was recognised, the previously recognised loss is reversed by adjusting the allowance. Once an impairment loss has been recognised on a financial asset or group of financial assets, interest income is recognised on the carrying amount using the rate of interest at which estimated future cash flows were discounted in measuring impairment.

Impaired loans and receivables are written off, i.e. the impairment provision is applied in writing down the loan's carrying value partially or in full, when the Group concludes that there is no longer any realistic prospect of recovery of part or all of the loan. For loans that are individually assessed for impairment, the timing of write off is determined on a case-by-case basis. Such loans are reviewed regularly and write off will be prompted by bankruptcy, insolvency, renegotiation and similar events.

The typical time frames from initial impairment to write off for the Group's collectively-assessed portfolios are:

- Retail mortgages: write off usually occurs within five years, or when an account is closed if earlier.
- Credit cards: the irrecoverable amount is written off after 12 months; three years later any remaining amounts outstanding are written off.
- Overdrafts and other unsecured loans: write off occurs within six years.
- Business and commercial loans: write offs of commercial loans are determined in the light of individual circumstances; the period does not exceed five years. Business loans are generally written off within five years.

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

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

16. Financial liabilities

Financial liabilities are recognised initially at fair value and classified into held-for-trading; designated as at fair value through profit or loss; or amortised cost. Issues of financial liabilities measured at amortised cost are recognised on settlement date; all other regular way transactions in financial liabilities are recognised on trade date.

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

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

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

Financial liabilities designated as at fair value through profit or loss principally comprise structured liabilities issued by the Group: designation significantly reduces the measurement inconsistency between these liabilities and the related derivatives carried at fair value.

Amortised cost - all other financial liabilities are measured at amortised cost using the effective interest method (see Accounting policy 3).

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

17. Financial guarantee contracts

Under a financial guarantee contract, the Group, in return for a fee, undertakes to meet a customer's obligations under the terms of a debt instrument if the customer fails to do so. A financial guarantee is recognised as a liability; initially at fair value and, if not designated as at fair value through profit or loss, subsequently at the higher of its initial value less cumulative amortisation and any provision under the contract measured in accordance with Accounting policy 12. Amortisation is calculated so as to recognise fees receivable in profit or loss over the period of the guarantee.

18. Loan commitments

Provision is made for loan commitments, other than those classified as held-for-trading, if it is probable that the facility will be drawn and the resulting loan will be recognised at an amount less than the cash advanced. Syndicated loan commitments in excess of the level of lending under the commitment approved for retention by the Group are classified as held-for-trading and measured at fair value.

19. Derecognition

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

A financial liability is removed from the balance sheet when the obligation is discharged, or is cancelled, or expires. On the redemption or settlement of debt securities (including subordinated liabilities) issued by the Group, the Group derecognises the debt instrument and records a gain or loss being the difference between the debt's carrying amount and the cost of redemption or settlement. The same treatment applies where the debt is exchanged for a new debt issue that has terms substantially different from those of the existing debt. The assessment of whether the terms of the new debt instrument are substantially different takes into account qualitative and quantitative characteristics including a comparison of the present value of the cash flows under the new terms with the present value of the remaining cash flows of the original debt issue discounted at the effective interest rate of the original debt issue.

20. Sale and repurchase transactions

Securities subject to a sale and repurchase agreement under which substantially all the risks and rewards of ownership are retained by the Group continue to be shown on the balance sheet and the sale proceeds recorded as a financial liability. Securities acquired in a reverse sale and repurchase transaction under which the Group is not exposed to substantially all the risks and rewards of ownership are not recognised on the balance sheet and the consideration paid is recorded as a financial asset.

Securities borrowing and lending transactions are usually secured by cash or securities advanced by the borrower. Borrowed securities are not recognised on the balance sheet or lent securities derecognised.

Cash collateral given or received is treated as a loan or deposit; collateral in the form of securities is not recognised. However, where securities borrowed are transferred to third parties, a liability for the obligation to return the securities to the stock lending counterparty is recorded.

21. Netting

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

22. Capital instruments

The Group classifies a financial instrument that it issues as a liability if it is a contractual obligation to deliver cash or another financial asset, or to exchange financial assets or financial liabilities on potentially unfavourable terms and as equity if it evidences a residual interest in the assets of the Group after the deduction of liabilities. The components of a compound financial instrument issued by the Group are classified and accounted for separately as financial assets, financial liabilities or equity as appropriate.

Incremental costs and related tax that are directly attributable to an equity transaction are deducted from equity.

The consideration for any ordinary shares of the company purchased by the Group (treasury shares) is deducted from equity. On the cancellation of treasury shares their nominal value is removed from equity and any excess of consideration over nominal value is treated in accordance with the capital maintenance provisions of the Companies Act. On the sale or reissue of treasury shares the consideration received and related tax are credited to equity, net of any directly attributable incremental costs.

23. Derivatives and hedging

Derivative financial instruments are initially recognised, and subsequently measured, at fair value. The Group's approach to determining the fair value of financial instruments is set out in the section of Critical accounting policies and key sources of estimation uncertainty entitled Fair value - financial instruments; further details are given in Note 9.

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

Gains and losses arising from changes in the fair value of derivatives that are not the hedging instrument in a qualifying hedge are recognised as they arise in profit or loss. Gains and losses are recorded in Income from trading activities except for gains and losses on those derivatives that are managed together with financial instruments designated at fair value; these gains and losses are included in Other operating income. The Group enters into three types of hedge relationship: hedges of changes in the fair value of a recognised asset or liability or unrecognised firm commitment (fair value hedges); hedges of the variability in cash flows from a recognised asset or liability or a highly probable forecast transaction (cash flow hedges); and hedges of the net investment in a foreign operation.

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

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

Cash flow hedge - in a cash flow hedge, the effective portion of the gain or loss on the hedging instrument is recognised in other comprehensive income and the ineffective portion in profit or loss. When the forecast transaction results in the recognition of a financial asset or financial liability, the cumulative gain or loss is reclassified from equity to profit or loss in the same periods in which the hedged forecast cash flows affect profit or loss. Otherwise the cumulative gain or loss is removed from equity and recognised in profit or loss at the same time as the hedged transaction. Hedge accounting is discontinued if the hedge no longer meets the criteria for hedge accounting; if the hedging instrument expires or is sold, terminated or exercised; if the forecast transaction is no longer expected to occur; or if hedge designation is revoked. On the discontinuance of hedge accounting (except where a forecast transaction is no longer expected to occur), the cumulative unrealised gain or loss is reclassified from equity to profit or loss when the hedged cash flows occur or, if the forecast transaction results in the recognition of a financial asset or financial liability, when the hedged forecast cash flows affect profit or loss. Where a forecast transaction is no longer expected to occur, the cumulative unrealised gain or loss is reclassified from equity to profit or loss immediately.

Hedge of net investment in a foreign operation - in the hedge of a net investment in a foreign operation, the portion of foreign exchange differences arising on the hedging instrument determined to be an effective hedge is recognised in other comprehensive income. Any ineffective portion is recognised in profit or loss. Non-derivative financial liabilities as well as derivatives may be the hedging instrument in a net investment hedge. On disposal or partial disposal of a foreign operation, the amount accumulated in equity is reclassified from equity to profit or loss.

24. Share-based compensation

The Group operates a number of share-based compensation schemes under which it awards RBSG shares and share options to its employees. Such awards are generally subject to vesting conditions: conditions that vary the amount of cash or shares to which an employee is entitled. Vesting conditions include service conditions (requiring the employee to complete a specified period of service) and performance conditions (requiring the employee to complete a specified period of service and specified performance targets to be met). Other conditions to which an award is subject are non-vesting conditions (such as a requirement to save throughout the vesting period).

The cost of employee services received in exchange for an award of shares or share options granted is measured by reference to the fair value of the shares or share options on the date the award is granted and takes into account non-vesting conditions and market performance conditions (conditions related to the market price of RBSG shares): an award is treated as vesting irrespective of whether any market performance condition or non-vesting condition is met. The fair value of options granted is estimated using valuation techniques which incorporate exercise price, term, risk-free interest rates, the current share price and its expected volatility. The cost is expensed on a straight-line basis over the vesting period (the period during which all the specified vesting conditions must be satisfied) with a corresponding increase in equity in an equity-settled award, or a corresponding liability in a cash-settled award. The cost is adjusted for vesting conditions (other than market performance conditions) so as to reflect the number of shares or share options that actually vest.

If an award is modified, the original cost continues to be recognised as if there had been no modification. Where modification increases the fair value of the award, this increase is recognised as an expense over the modified vesting period. A new award of shares or share options is treated as the modification of a cancelled award if, on the date the new award is granted, the Group identifies them as replacing the cancelled award. The cancellation of an award through failure to meet non-vesting conditions triggers an immediate expense for any unrecognised element of the cost of an award.

25. Cash and cash equivalents

In the cash flow statement, cash and cash equivalents comprises cash and deposits with banks with an original maturity of less than three months together with short-term highly liquid investments that are readily convertible to known amounts of cash and subject to insignificant risk of change in value.

26. Shares in Group entities

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

Critical accounting policies and key sources of estimation uncertainty

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. UK company law and IFRS require the directors, in preparing the Group's financial statements, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. In the absence of an applicable standard or interpretation, IAS 8 'Accounting Policies, Changes in Accounting Estimates and Errors', requires management to develop and apply an accounting policy that results in relevant and reliable information in the light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB's 'Conceptual Framework for Financial Reporting'. The judgements and assumptions involved in the Group's accounting policies that are considered by the Board to be the most important to the portrayal of its financial condition are discussed below. The use of estimates, assumptions or models that differ from those adopted by the Group would affect its reported results.

(i) Pensions

The Group operates a number of defined benefit pension schemes as described in Note 4 on the accounts. As described in Accounting policy 5, the assets of the schemes are measured at their fair value at the balance sheet date. Scheme liabilities are measured using the projected unit credit method, which takes account of projected earnings increases, using actuarial assumptions that give the best estimate of the future cash flows that will arise under the scheme liabilities. These cash flows are discounted at the interest rate applicable to high-quality corporate bonds of the same currency and term as the liabilities. Any recognisable surplus or deficit of scheme assets over liabilities is recorded in the balance sheet as an asset (surplus) or liability (deficit).

In determining the value of scheme liabilities, financial and demographic assumptions are made including price inflation, pension increases, earnings growth and the longevity of scheme members. A range of assumptions could be adopted in valuing the schemes' liabilities. Different assumptions could significantly alter the amount of the surplus or deficit recognised in the balance sheet and the pension cost charged to the income statement. The assumptions adopted for the Group's pension schemes are set out in Note 4 on the accounts, together with sensitivities of the balance sheet and income statement to changes in those assumptions.

A pension asset of £215 million and a liability of £3,764 million were recognised on the balance sheet at 31 December 2015 (2014 - asset £180 million, liability £4,289 million).

(ii) Goodwill

The Group capitalises goodwill arising on the acquisition of businesses, as discussed in Accounting policy 6. The carrying value of goodwill as at 31 December 2015 was £5,549 million (2014 - £6,255 million).

Goodwill is the excess of the cost of an acquired business over the fair value of its net assets. Goodwill is not amortised but is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired.

Impairment testing in accordance with Accounting policy 8 above inherently involves a number of judgmental areas: the preparation of cash flow forecasts for periods that are beyond the normal requirements of management reporting; the assessment of the discount rate appropriate to the business; estimation of the fair value of cash-generating units; and the valuation of their separable assets. The sensitivity of the assessment to changes in assumptions is discussed in Note 16.

(iii) Provisions for liabilities

As set out in Note 21, at 31 December 2015 the Group recognised provisions for liabilities in respect of Payment Protection Insurance, £996 million (2014 - £799 million), foreign exchange investigations, £306 million (2014 - £320 million), other customer redress, £610 million (2014 - £568 million) and other regulatory proceedings and litigation, £3,964 million (2014 - £1,955 million). Provisions are liabilities of uncertain timing or amount, and are recognised when there is a present obligation as a result of a past event, the outflow of economic benefit is probable and the outflow can be estimated reliably. Judgement is involved in determining whether an obligation exists, and in estimating the probability, timing and amount of any outflows. Where the Group can look to another party such as an insurer to pay some or all of the expenditure required to settle a provision, any reimbursement is recognised when, and only when, it is virtually certain that it will be received.

Payment Protection Insurance - the Group has established a provision for redress payable in respect of the mis-selling of Payment Protection Insurance policies. The provision is management's best estimate of the anticipated costs of redress and related administration expenses. The determination of appropriate assumptions to underpin the provision requires significant judgement by management. The principal assumptions underlying the provision together with sensitivities to changes in those assumptions are given in Note 21.

Provisions for litigation - the Group and members of the Group are party to legal proceedings in the United Kingdom, the United States and other jurisdictions, arising out of their normal business operations. The measurement and recognition of liabilities in respect of litigation involves a high degree of management judgement. Before the existence of a present obligation as the result of a past event can be confirmed, numerous facts may need to be established, involving extensive and time-consuming discovery, and novel or unsettled legal questions addressed. Once it is determined there is an obligation, assessing the probability of economic outflows and estimating the amount of any liability can be very difficult. In many proceedings, it is not possible to determine whether any loss is probable or to estimate the amount of any loss. Furthermore, for an individual matter, there can be a wide range of possible outcomes and often it is not practicable to quantify a range of such outcomes. The Group's outstanding litigation is periodically assessed in consultation with external professional advisers, where appropriate, to determine the likelihood of the Group incurring a liability. A detailed description of the Group's material legal proceedings and a discussion of the nature of the associated uncertainties are given in Note 29.

Tax contingencies - determining the Group's income tax charge and its provisions for income taxes necessarily involves a significant degree of estimation and judgement. The tax treatment of some transactions is uncertain and tax computations are yet to be agreed with the tax authorities in a number of jurisdictions. The Group recognises anticipated tax liabilities based on all available evidence and, where appropriate, in the light of external advice. Any difference between the final outcome and the amounts provided will affect current and deferred income tax assets and liabilities in the period when the matter is resolved.

(iv) Deferred tax

The Group makes provision for deferred tax on temporary differences where tax recognition occurs at a different time from accounting recognition. Deferred tax assets of £2,622 million were recognised as at 31 December 2015 (2014 - £1,881 million).

The Group has recognised deferred tax assets in respect of losses, principally in the UK, and temporary differences. Deferred tax assets are recognised in respect of unused tax losses and other temporary differences to the extent that it is probable that there will be future UK taxable profits against which the losses and other temporary differences can be utilised. The Group has considered the carrying value of the deferred tax asset as at 31 December 2015 and concluded that it is recoverable based on future projections.

Deferred tax assets of £4,364 million (2014 - £3,778 million) have not been recognised in respect of tax losses and other temporary differences where the availability of future taxable profits is uncertain. Further details about the Group's deferred tax assets are given in Note 22.

(v) Loan impairment provisions

The Group's loan impairment provisions are established to recognise incurred impairment losses in its portfolio of loans classified as loans and receivables and carried at amortised cost in accordance with Accounting policy 15.

A loan is impaired when there is objective evidence that events since the loan was granted have affected expected cash flows from the loan. Such objective evidence, indicative that a borrower's financial condition has deteriorated, can include for loans that are individually assessed: the non-payment of interest or principal; debt renegotiation; probable bankruptcy or liquidation; significant reduction in the value of any security; breach of limits or covenants; and deteriorating trading performance and, for collectively assessed portfolios: the borrowers' payment status and observable data about relevant macroeconomic measures.

The impairment loss is the difference between the carrying value of the loan and the present value of estimated future cash flows at the loan's original effective interest rate.

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

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

Collective component - this is made up of two elements: loan impairment provisions for impaired loans that are below individual assessment thresholds (collectively assessed provisions) and for loan losses that have been incurred but have not been separately identified at the balance sheet date (latent loss provisions). Collectively assessed provisions are established on a portfolio basis using a present value methodology taking into account the level of arrears, security, past loss experience, credit scores and defaults based on portfolio trends. The most significant factors in establishing these provisions are the expected loss rates and the related average life. These portfolios include mortgages, credit card receivables and other personal lending. The future credit quality of these portfolios is subject to uncertainties that could cause actual credit losses to differ materially from reported loan impairment provisions. These uncertainties include the economic environment, notably interest rates and their effect on customer spending, the unemployment level, payment behaviour and bankruptcy trends. Latent loss provisions are held against estimated impairment losses in the performing portfolio that have yet to be identified as at the balance sheet date. To assess the latent loss within its portfolios, the Group has developed methodologies to estimate the time that an asset can remain impaired within a performing portfolio before it is identified and reported as such.

(vi) Fair value - financial instruments

In accordance with Accounting policies 14, 16 and 23, financial instruments classified as held-for-trading or designated as at fair value through profit or loss and financial assets classified as available-for-sale are recognised in the financial statements at fair value. All derivatives are measured at fair value.

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. A fair value measurement takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. It also uses the assumptions that market participants would use when pricing the asset or liability. In determining fair value the Group maximises the use of relevant observable inputs and minimises the use of unobservable inputs.

Where the Group manages a group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, it measures the fair value of a group of financial assets and financial liabilities on the basis of the price that it would receive to sell a net long position (i.e. an asset) for a particular risk exposure or to transfer a net short position (i.e. a liability) for a particular risk exposure in an orderly transaction at the measurement date under current market conditions.

Credit valuation adjustments are made when valuing derivative financial assets to incorporate counterparty credit risk. Adjustments are also made when valuing financial liabilities measured at fair value to reflect the Group's own credit standing.

Where the market for a financial instrument is not active, fair value is established using a valuation technique. These valuation techniques involve a degree of estimation, the extent of which depends on the instrument's complexity and the availability of market-based data. Further details about the Group's valuation methodologies and the sensitivity to reasonably possible alternative assumptions of the fair value of financial instruments valued using techniques where at least one significant input is unobservable are given in Note 9.

Accounting developments

International Financial Reporting Standards

A number of IFRSs and amendments to IFRS were in issue at 31 December 2015 that would affect RBS Group from 1 January 2016 or later.

Effective for 2016

'Accounting for Acquisitions of Interests in Joint Operations' issued in May 2014 amends IFRS 11 'Joint Arrangements. An acquirer of an interest in a joint operation that is a business applies the relevant principles for business combinations in IFRS 3 and other standards and makes the relevant disclosures accordingly. The effective date is 1 January 2016.

'Clarification of Acceptable Methods of Depreciation and Amortisation' issued in May 2014 amends IAS 16 'Property, Plant and Equipment' and IAS 38 'Intangible Assets' requiring amortisation to be based on the consumption of an asset, introducing a rebuttable presumption that this is not achieved by an amortisation profile aligned to revenue. The effective date is 1 January 2016.

Annual Improvements to IFRS 2012 - 2014 cycle was issued in September 2014 making a number of minor amendments to IFRS. Its effective date is 1 January 2016.

Amendments to IFRS 10 'Consolidated Financial Statements', IFRS 12 'Disclosure of Interests in Other Entities' and IAS 28 'Investments in Associates and Joint Ventures' were issued in September 2014 to clarify the accounting for sales between an investor, its associate or joint ventures, and in December 2014 to clarify the application of the investment entity consolidation exception. The September 2014 amendments will be effective from a date to be determined by the IASB and the December 2014 amendments from 1 January 2016.

An amendment to IAS 1 'Presentation of Financial Statements' was issued in December 2014 to clarify the application of materiality to financial statements. Its effective date is 1 January 2016.

None of these amendments is expected to have a material effect on the Group's financial statements.

Effective after 2016 - IFRS 9

In July 2014, the IASB published IFRS 9 'Financial Instruments' with an effective date of 1 January 2018. IFRS 9 replaces the current financial instruments standard IAS 39, setting out new accounting requirements in a number of areas. The Group is continuing its assessment of the standard's effect on its financial statements.

The principle features of IFRS 9 are as follows:

Recognition and derecognition

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

Classification and measurement

Financial assets - There are three classifications for financial assets in IFRS 9: fair value through profit or loss; fair value through other comprehensive income; and amortised cost.

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

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

The Group continues to evaluate the overall effect, but expects that the measurement basis of the majority of the Group's financial assets will be unchanged on application of IFRS 9.

Financial liabilities - IFRS 9's requirements on the classification and measurement of financial liabilities are largely unchanged from those in IAS 39. However, there is a change to the treatment of changes in the fair value attributable to own credit risk of financial liabilities designated as at fair value through profit or loss which are recognised in other comprehensive income and not in profit or loss as required by IAS 39.

Hedge accounting

Hedge accounting requirements are designed to align accounting more closely to the risk management framework; permit a greater variety of hedging instruments; and remove or simplify some of the rule-based requirements in IAS 39. The basic mechanics of hedge accounting: fair value, cash flow and net investment hedges are retained. There is an option in IFRS 9 for an accounting policy choice to continue with the IAS 39 hedge accounting framework. The Group is actively considering its implementation approach.

Credit impairment

IFRS 9's credit impairment requirements apply to financial assets measured at amortised cost, to those measured at fair value through other comprehensive income, to lease receivables and to certain loan commitments and financial guarantee contracts. On initial recognition a loss allowance is established at an amount equal to 12-month expected credit losses ('ECL') that is the portion of life-time expected losses resulting from default events that are possible within the next 12 months. Where a significant increase in credit risk since initial recognition is identified, the loss allowance increases so as to recognise all expected default events over the expected life of the asset. The Group expects that financial assets where there is objective evidence of impairment under IAS39 will be credit impaired under IFRS 9, and carry loss allowances based on all expected default events.

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

A single bank-wide programme has been established to implement the necessary changes in the modelling of credit loss parameters, and the underlying credit management and financial processes; this programme is led jointly by Risk and Finance. The inclusion of loss allowances on all financial assets will tend to result in an increase in overall impairment balances when compared with the existing basis of measurement under IAS 39.

Transition

The classification and measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application, with no requirement to restate comparative periods. Hedge accounting is generally applied prospectively from that date.

Effective after 2016 - other standards

In January 2016, the IASB amended IAS 7 'Cash Flow Statements' to require disclosure of the movements in financing liabilities. The amendment is effective from1 January 2017.

In January 2016, the IASB amended IAS 12 'Income taxes' to clarify the recognition of deferred tax assets in respect of unrealised losses. The amendment is effective from 1 January 2017.

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

IFRS 16 'Leases' was issued in January 2016 to replace IAS 17 'Leases'. Accounting for finance leases will remain substantially the same. Operating leases will be brought on balance sheet through the recognition of assets representing the contractual rights of use and liabilities will be recognised for the contractual payments. The effective date is 1 January 2019.

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

1 Net interest income

	2015 £m	2014 £m	2013 £m
Loans and advances to customers	11,155	12,143	12,987
Loans and advances to banks	370	358	481
Debt securities	221	304	683
Interest receivable	11,746	12,805	14,151
Customer accounts: demand deposits	617	589	659
Customer accounts: savings deposits	439	719	1,281
Customer accounts: other time deposits	281	379	631
Deposits by banks	65	85	204
Debt securities in issue	569	788	1,104
Subordinated liabilities	1,261	1,292	1,305
Internal funding of trading businesses	106	87	337
Interest payable	3,338	3,939	5,521
Net interest income	8,408	8,866	8,630

2 Non-interest income

	2015 £m	2014 £m	2013 £m
Fees and commissions receivable			
Payment services	921	987	1,079
Credit and debit card fees	738	822	888
Lending (credit facilities)	1,074	1,242	1,279
Brokerage	260	318	389
Investment management	256	342	385
Trade finance	235	268	243
Other	208	341	335
	3,692	4,320	4,598
Fees and commissions payable	(805)	(842)	(892)
Income from trading activities			
Foreign exchange	769	1,330	1,821
Interest rate	11	(224)	87
Credit	(78)	3	595
Changes in fair value of own debt and derivative liabilities attributable to own credit			
- debt securities in issue	247	44	133
- derivative liabilities	2	(77)	(84)
Equities and other	3	114	308
	954	1,190	2,860
(Loss)/gain on redemption of own debt	(263)	6	162
Other operating income			
Operating lease and other rental income	276	379	483
Changes in the fair value of own debt designated as at fair value through profit or loss attributable to own credit risk (1)			
- debt securities in issue	83	(86)	(35)
- subordinated liabilities	(3)	(9)	(39)
Other changes in the fair value of other financial assets and liabilities designated as at fair value through profit or loss and related derivatives	246	53	(44)
Changes in the fair value of investment properties	13	(25)	(281)
Profit on sale of securities	40	387	942
Profit on sale of property, plant and equipment	88	138	36
(Loss)/profit on sale of subsidiaries and associates	(158)	(30)	179
Loss on disposal or settlement of loans and receivables	(551)	(236)	(137)
Share of profits of associated entities	27	30	(1)
Other income (2)	104	477	294
	165	1,078	1,397

Notes:
(1) Measured as the change in fair value from movements in the year in the credit risk premium payable by the Group.
(2) Includes income from activities other than banking.

3 Operating expenses

	2015 £m	2014 £m	2013 £m
Wages, salaries and other staff costs	4,763	4,722	4,904
Social security costs	342	376	414
Share-based compensation	36	43	49
Pension costs			
- defined benefit schemes (see Note 4)	521	459	504
- curtailment and settlement gains (see Note 4)	(65)	—	(3)
- defined contribution schemes	71	83	61
Staff costs	5,668	5,683	5,929
Premises and equipment	1,809	2,059	1,994
Other administrative expenses (1)	6,160	4,361	6,530
Property, plant and equipment depreciation and write down (see Note 17)	944	664	746
Intangible assets amortisation (see Note 16)	229	262	363
Depreciation and amortisation	1,173	926	1,109
Write down of goodwill and other intangible assets (see Note 16)	1,331	523	423
	16,141	13,552	15,985

Integration, restructuring and divestment costs

Included in operating expenses are the following integration, restructuring and divestment costs.

	Staff £m	Premises and depreciation £m	Other (2) £m	Total £m
Integration and restructuring				
2015	598	733	944	2,275
2014	261	269	268	798
2013	173	103	131	407
Divestment				
2015	214	9	405	628
2014	120	3	233	356
2013	86	2	77	165

Notes:
(1) Includes Payment Protection Insurance costs, Interest Rate Hedging Products redress and related costs, other litigation and conduct costs and UK bank levy. Further details are provided in Note 21.
(2) Includes other administrative expenses, write down of goodwill and other intangible assets.

The average number of persons employed, rounded to the nearest hundred, by the Group during the year, excluding temporary staff, was 87,400 (2014 - 90,800; 2013 - 91,200); on the same basis, there were 10,100 people employed in discontinued operations (2014 - 18,200; 2013 - 19,200). The number of persons employed by the Group in continuing operations at 31 December, excluding temporary staff, was as follows:

	Group		
	2015	2014*	2013*
UK Personal & Business Banking	24,600	24,500	26,100
Ulster Bank RoI	2,500	2,500	2,600
Personal & Business Banking	27,100	27,000	28,700
Commercial Banking	5,700	6,000	7,000
Private Banking	1,900	2,200	2,200
RBS International	700	600	700
Commercial & Private Banking	8,300	8,800	9,900
Corporate & Institutional Banking	1,200	1,700	2,100
Capital Resolution	1,000	1,900	1,900
Williams & Glyn	4,800	4,500	4,600
Central & Other	44,600	44,000	45,700
Non-Core	n/a	n/a	800
Total	87,000	87,900	93,700
UK	64,100	63,400	68,700
USA	1,100	2,000	2,300
Europe	6,100	7,400	8,200
Rest of the World	15,700	15,100	14,500
Total	87,000	87,900	93,700

*Re-presented to reflect the segmental reorganisation

There were no people employed in discontinued operations at 31 December 2015 (2014 -17,400; 2013 - 19,000).

Share-based payments

As described in the Remuneration report in the RBS Group Annual Report and Accounts 2015, the RBS Group grants share-based awards to employees principally on the following bases:

Award plan	Eligible employees	Nature of award (1)	Vesting conditions (2)	Settlement
Sharesave	UK, Republic of Ireland, Channel Islands, Gibraltar and Isle of Man	Option to buy shares under employee savings plan	Continuing employment or leavers in certain circumstances	2016 to 2020
Deferred performance awards	All	Awards of ordinary shares	Continuing employment or leavers in certain circumstances	2016 to 2018
Long-term incentives (3)	Senior employees	Awards of conditional shares or share options	Continuing employment or leavers in certain circumstances and/or achievement of performance conditions	2016 to 2020

Notes:
(1) Awards are equity-settled unless international comparability is better served by cash-settled awards.
(2) All awards have vesting conditions and therefore some may not vest.
(3) Long-term incentives include the Executive Share Option Plan, the Long-Term Incentive Plan, the Medium-Term Performance Plan and the Employee Share Plan.

The fair value of options granted in 2015 was determined using a pricing model that included: expected volatility of shares determined at the grant date based on historical volatility over a period of up to seven years; expected option lives that equal the vesting period; no dividends on equity shares; and risk-free interest rates determined from UK gilts with terms matching the expected lives of the options.

The strike price of options and the fair value on granting awards of fully paid shares is the average market price over the five trading days (three trading days for Sharesave) preceding grant date.

Sharesave

	2015		2014		2013	
	Average exercise price £	Shares under option (million)	Average exercise price £	Shares under option (million)	Average exercise price £	Shares under option (million)
At 1 January	2.85	51	2.90	62	2.86	57
Granted	2.91	12	3.43	12	2.96	13
Exercised	2.38	(2)	2.34	(6)	2.36	—
Cancelled	2.98	(5)	3.61	(17)	3.38	(8)
At 31 December	2.87	56	2.85	51	2.90	62

Options are exercisable within six months of vesting; 1.0 million options were exercisable at 31 December 2015 (2014 - 1.9 million; 2013 - 1.3 million). The weighted average share price at the date of exercise of options was £3.54 (2014 - £3.65; 2013 - £3.36). At 31 December 2015, exercise prices ranged from £2.33 to £18.93 (2014 and 2013 - £2.33 to £39.27) and the remaining average contractual life was 2.9 years (2014 - 3.7 years; 2013 - 3.5 years). The fair value of options granted in 2015 was £12 million (2014 - £18 million; 2013 - £25 million).

Deferred performance awards

	2015		2014		2013	
	Value at grant £m	Shares awarded (million)	Value at grant £m	Shares awarded (million)	Value at grant £m	Shares awarded (million)
At 1 January	272	85	180	55	261	73
Granted	186	50	311	95	113	36
Forfeited	(34)	(11)	(28)	(7)	(48)	(14)
Vested	(148)	(44)	(170)	(51)	(146)	(40)
Disposals	—	—	(21)	(7)	—	—
At 31 December	276	80	272	85	180	55

The awards granted in 2015 vest evenly over the following three anniversaries.

Long-term incentives

	2015			2014			2013		
	Value at grant £m	Shares awarded (million)	Options over shares (million)	Value at grant £m	Shares awarded (million)	Options over shares (million)	Value at grant £m	Shares awarded (million)	Options over shares (million)
At 1 January	214	69	7	320	94	13	375	98	20
Granted	39	11	—	72	22	—	109	35	—
Vested/exercised	(51)	(18)	(2)	(61)	(14)	(5)	(51)	(11)	(3)
Lapsed	(49)	(18)	—	(85)	(22)	(1)	(113)	(28)	(4)
Disposal	—	—	—	(32)	(11)	—	—	—	—
At 31 December	153	44	5	214	69	7	320	94	13

The market value of awards vested/exercised in 2015 was £55 million (2014 - £44 million; 2013 - £37 million). There are vested options over 5 million shares exercisable up to 2019 (2014 - 7 million; 2013 - 13 million).

4 Pensions

The Group sponsors a number of pension schemes in the UK and overseas.

The Royal Bank of Scotland Group Pension Fund (the "Main scheme") operates under UK trust law and is managed and administered on behalf of its members in accordance with the terms of the trust deed, the scheme rules and UK legislation (principally the Pension Schemes Act 1993, the Pensions Act 1995 and the Pensions Act 2004). Under UK legislation a defined benefit pension scheme is required to meet the statutory funding objective of having sufficient and appropriate assets to cover its liabilities. Pension fund trustees are required to: prepare a statement of funding principles; obtain regular actuarial valuations and reports; put in place a recovery plan addressing any funding shortfall; and send regular summary funding statements to members of the scheme.

The Main scheme corporate trustee is RBS Pension Trustee Limited (RBSPT), a wholly owned subsidiary of National Westminster Bank Plc. RBSPT is the legal owner of the Main scheme assets which are held separately from the assets of the Group. The Board of RBSPT comprises four trustee directors nominated by members selected from eligible active staff and pensioner members who apply and six appointed by the Group. The Board is responsible for operating the scheme in line with its formal rules and pensions law. It has a duty to act in the best interests of all scheme members, including pensioners and those who are no longer employed by the Group, but who still have benefits in the scheme.

Similar governance principles apply to the Group's other pension schemes, although different legislative frameworks apply to the Group's overseas schemes.

The Main scheme accounting for 88% (2014 - 87%) of the Group's retirement benefit obligations, was closed to new entrants in 2006. Since 2009, pensionable salary increases in the Main scheme and certain other UK and Irish schemes have been limited to 2% per annum or CPI inflation if lower. Also with effect from 1 October 2012, the normal pension age for future benefits was increased to 65 unless members elected to contribute to maintain a normal pension age of 60.

The Group's defined benefit schemes generally provide a pension of one-sixtieth of final pensionable salary for each year of service prior to retirement up to a maximum of 40 years. Employees making additional contributions can secure additional benefits.

Since October 2006, new UK entrants may join The Royal Bank of Scotland Retirement Savings Plan, a defined contribution pension scheme.

The Group also provides post-retirement benefits other than pensions, principally through subscriptions to private healthcare schemes in the UK and unfunded post-retirement benefit plans. Provision for the costs of these benefits is charged to the income statement over the average remaining future service lives of eligible employees. The amounts are not material.

Interim valuations of the Group's schemes under IAS 19 'Employee Benefits' were prepared at 31 December with the support of independent actuaries, using the following assumptions:

	Main scheme	
Principal IAS 19 actuarial assumptions	2015 %	2014 %
Discount rate	3.9	3.7
Expected return on plan assets	3.9	3.7
Rate of increase in salaries	1.8	1.8
Rate of increase in pensions in payment	2.8	2.8
Inflation assumption (RPI)	3.0	3.0

Discount rate

The Group discounts its defined benefit pension obligations at discount rates determined by reference to the yield on 'high quality' corporate bonds.

The sterling yield curve (applied to 95% of the Group's defined benefit obligations) is constructed by reference to yields on 'AA' corporate bonds from which a single discount rate is derived based on a cash flow profile similar in structure and duration to the pension obligations. Significant judgement is required when setting the criteria for bonds to be included in the population from which the yield curve is derived.

The criteria include issue size, quality of pricing and the exclusion of outliers. Judgement is also required in determining the shape of the yield curve at long durations: a constant credit spread relative to gilts is assumed.

Major classes of plan assets as a percentage of total plan assets	Main scheme 2015 %	Main scheme 2014 %
Quoted assets		
Quoted equities		
- Consumer industry	5.3	4.3
- Manufacturing industry	3.2	3.2
- Energy and utilities	2.6	2.9
- Financial institutions	5.4	3.9
- Technology and telecommunications	3.4	4.2
- Other	0.9	2.8
Private equity	3.4	4.3
Index-linked bonds	28.2	28.1
Government fixed interest bonds	9.0	3.6
Corporate fixed interest bonds	18.0	15.3
Unquoted assets		
Corporate and other bonds	3.3	2.3
Hedge funds	0.2	1.6
Real estate	6.4	5.8
Derivatives	6.4	10.6
Cash and other assets	4.1	7.1
Equity exposure of equity futures	(1.4)	1.3
Cash exposure of equity futures	1.6	(1.3)
	100.0	100.0

The assets of the Main scheme, which represent 88% of plan assets at 31 December 2015 (2014 - 88%), are invested in a diversified portfolio of quoted and private equity, government and corporate fixed-interest and index-linked bonds, and other assets including property and hedge funds.

The Main scheme employs derivative instruments to achieve a desired asset class exposure or to match assets more closely to liabilities. The value of assets shown reflects the assets owned by the scheme, with any derivative holdings valued on a mark-to-market basis.

The Main scheme's holdings of derivative instruments are summarised in the table below:

	2015			2014		
	Notional amounts £m	Fair value Assets £m	Fair value Liabilities £m	Notional amounts £m	Fair value Assets £m	Fair value Liabilities £m
Inflation rate swaps	9,018	76	647	8,467	73	415
Interest rate swaps	15,739	5,722	3,710	23,858	6,055	3,305
Currency forwards	10,247	—	222	8,562	2	—
Equity and bond call options	6,277	744	1	7,382	846	48
Equity and bond put options	6,109	2	12	7,409	1	61
Other	2,236	1,506	1,479	2,437	665	628

The investment strategy of other schemes is similar to that of the Main scheme, adjusted to take account of the nature of liabilities, risk appetite of the trustees, size of the scheme and any local regulatory constraints. The use of derivative instruments outside the Main scheme is not material.

Swaps are part of the management of the inflation and interest rate sensitivity of the Main scheme liabilities. They have been executed at prevailing market rates and within standard market bid/offer spreads with a number of banks, including The Royal Bank of Scotland plc and National Westminster Bank Plc (the "banks"). At 31 December 2015, the gross notional value of the swaps was £26,871 million (2014 - £34,163 million) and had a net positive fair value of £1,444 million (2014 - £2,433 million).

Collateral is required on all swap transactions. The banks had delivered £1,267 million of collateral at 31 December 2015 (2014 - £2,908 million).

Ordinary shares of the company with a fair value of £2 million (2014 - £2 million) and other financial instruments issued by the Group with a value of £1,144 million (2014 - £2,172 million) are held by the Main scheme.

IAS 19 post-retirement mortality assumptions (Main scheme)	2015	2014
Longevity at age 60 for current pensioners (years)		
Males	27.8	28.0
Females	29.8	30.0
Longevity at age 60 for future pensioners currently aged 40 (years)		
Males	29.1	29.3
Females	31.4	31.6

Changes in value of net pension deficit*	Fair value of plan assets £m	Present value of defined benefit obligations £m	Asset ceiling/ minimum funding (1) £m	Net pension deficit £m
At 1 January 2014	28,471	31,445	—	2,974
Change in accounting policy	—	—	105	105
Currency translation and other adjustments	(63)	(86)	—	(23)
Income statement				
Net interest expense	1,314	1,419	—	105
Current service cost	—	356	—	356
Past service cost	—	2	—	2
	1,314	1,777	—	463
Statement of comprehensive income				
Return on plan assets above recognised interest income	5,171	—	—	(5,171)
Experience gains and losses	—	(18)	—	(18)
Effect of changes in actuarial financial assumptions	—	4,799	—	4,799
Effect of changes in actuarial demographic assumptions	—	490	—	490
Asset ceiling/minimum funding adjustments	—	—	1,749	1,749
	5,171	5,271	1,749	1,849
Contributions by employer	1,063	—	—	(1,063)
Contributions by plan participants and other scheme members	5	5	—	—
Benefits paid	(1,026)	(1,026)	—	—
Transfers to disposal groups	(594)	(790)	—	(196)
At 1 January 2015	34,341	36,596	1,854	4,109
Currency translation and other adjustments	(31)	(63)	—	(32)
Income statement				
Net interest expense	1,206	1,295	64	153
Current service cost	—	328	—	328
Past service cost	—	40	—	40
Gains on settlements	—	(65)	—	(65)
	1,206	1,598	64	456
Statement of comprehensive income				
Return on plan assets above recognised interest income	(457)	—	—	457
Experience gains and losses	—	(258)	—	(258)
Effect of changes in actuarial financial assumptions	—	(1,386)	—	(1,386)
Effect of changes in actuarial demographic assumptions	—	48	—	48
Asset ceiling/minimum funding adjustments	—	—	1,212	1,212
	(457)	(1,596)	1,212	73
Contributions by employer	1,059	—	—	(1,059)
Contributions by plan participants and other scheme members	6	6	—	—
Benefits paid	(1,129)	(1,129)	—	—
Transfers to disposal groups	(299)	(297)	—	2
At 31 December 2015	34,696	35,115	3,130	3,549

Note:
(1) In recognising the net surplus or deficit of a pension scheme, the funded status of each scheme is adjusted to reflect any minimum funding requirement imposed on the sponsor and any ceiling on the amount that the sponsor has a right to recover from a scheme.

Net pension deficit comprises	2015 £m	2014* £m
Net assets of schemes in surplus (included in Prepayments, accrued income and other assets, Note 18)	(215)	(180)
Net liabilities of schemes in deficit	3,764	4,289
	3,549	4,109

* Restated - refer to page 148 for further details

Analysis of net pension deficit	Main scheme 2015 £m	2014 £m
Fund assets at fair value	30,703	30,077
Present value of fund liabilities	30,966	31,776
Funded status	263	1,699
Asset ceiling/minimum funding	2,981	1,739
Retirement benefit liability	3,244	3,438
Minimum funding requirement	3,657	4,190
Asset ceiling	(413)	(752)
	3,244	3,438

The income statement charge comprises:

	2015 £m	2014 £m	2013 £m
Continuing operations	456	459	501
Discontinued operations	—	4	9
	456	463	510

The weighted average duration of the Main Scheme's defined benefit obligation at 31 December 2015 is 19.1 years (2014 - 20.0 years).

The defined benefit obligation is attributable to the different classes of scheme members in the following proportions (Main scheme):

	2015 %	2014 %
Active	17.5	18.8
Deferred	41.9	41.0
Pensioner	40.6	40.2
	100.0	100.0

The table below sets out the sensitivities of the present value of defined benefit obligations at 31 December to a change in the principal actuarial assumptions.

	Main scheme (decrease)/increase in obligation at 31 December	
	2015 £m	2014 £m
0.25% increase in the discount rate	(1,392)	(1,466)
0.25% increase in inflation	1,106	1,159
0.25% additional rate of increase in pensions in payment	945	982
Longevity increase of one year	853	988

Pension liabilities are calculated on the central assumptions and under the relevant sensitivity scenarios. The sensitivity to pension liabilities is the difference between these calculations.

The sensitivity analysis presented above may not be representative of the actual change in the defined benefit obligation as it is unlikely that the changes in assumptions would occur in isolation of one another as some of the assumptions may be correlated.

History of defined benefit schemes	Group 2015 £m	2014 £m	2013 £m	2012 £m	2011 £m
Fair value of plan assets	34,696	34,341	28,471	26,359	23,830
Present value of defined benefit obligations	35,115	36,596	31,445	30,069	25,994
Net deficit	419	2,255	2,974	3,710	2,164
Experience gains/(losses) on plan liabilities	258	18	177	(202)	(224)
Experience gains on plan assets	(457)	5,171	1,097	476	812
Actual return on pension schemes assets	749	6,485	2,270	1,662	1,973
Actual return on pension schemes assets - %	2.2%	22.8%	8.6%	7.0%	9.1%

Triennial funding valuation

In May 2014, the triennial funding valuation of the Main scheme was agreed which showed that the value of the liabilities exceeded the value of assets by £5.6 billion at 31 March 2013, a ratio of 82%. To eliminate this deficit, RBS Group agreed to pay annual additional contributions of £650 million from 2014 to 2016 and £450 million (indexed in line with inflation) from 2017 to 2023. These contributions are in addition to regular annual contributions of approximately £270 million in respect of the ongoing accrual of benefits as well as contributions to meet the expenses of running the scheme.

In January 2016, RBS Group sought regulatory approval to accelerate the settlement of the outstanding additional contributions of £4.2 billion and it entered into a Memorandum of Understanding with the trustee of the Main scheme which, among other things, will bring forward the date of the next triennial funding valuation to no later than 31 December 2015.

The trustee of the Main scheme is responsible for setting the actuarial assumptions used in the triennial funding valuation having taken advice from the Scheme Actuary. These represent the trustee's prudent estimate of the future experience of the Main scheme taking into account the covenant provided by RBS Group and investment strategy of the scheme. They are agreed with RBS Group and documented in the Statement of Funding Principles.

The key assumption methodology used at 31 March 2013 valuation is set out below:

Principal actuarial assumptions

Discount rate	Fixed interest swap yield curve plus 1.5% per annum at all durations	
Inflation assumption	Retail price index (RPI) swap yield curve	
Rate of increase in pensions in payment	(RPI floor 0%, cap 5%): Limited price indexation (LPI) (0,5) swap yield curve	
Post retirement mortality assumptions:		
Longevity at age 60 for current pensioners (years)	Male	28.8
	Female	30.8
Longevity at age 60 for future pensioners currently aged 40 (years)	Male	30.7
	Female	32.9

5 Auditor's remuneration

Amounts paid to the Group's auditors for statutory audit and other services are set out below:

	Group	
	2015 £m	2014 £m
Fees payable for the audit of the Group's annual accounts	6.8	6.7
Fees payable to the auditor and its associates for other services to the Group		
- the audit of the Bank's subsidiaries pursuant to legislation	9.2	10.4
Total audit and audit-related assurance service fees	16.0	17.1

Fees payable to the auditor for non-audit services are disclosed in the consolidated financial statements of The Royal Bank of Scotland Group plc.

6 Tax

	Group		
	2015 £m	2014 £m	2013 £m
Current tax			
Charge for the year	(117)	(275)	(237)
Over/(under) provision in respect of prior years	235	75	(50)
	118	(200)	(287)
Deferred tax			
Credit/(charge) for the year arising from UK tax rate changes	94	—	(338)
Other (charges)/credits for the year	(187)	(355)	837
Reduction in the carrying value of deferred tax assets	—	(1,472)	(701)
Over/(under) provision in respect of prior year	4	(6)	182
Tax credit/(charge) for the year	29	(2,033)	(307)

The actual tax credit/(charge) differs from the expected tax credit/(charge) computed by applying the standard rate of UK corporation tax of 20.25% (2014 - 21.50%; 2013 - 23.25%) as follows:

	2015 £m	2014 £m	2013 £m
Expected tax credit/(charge)	638	(517)	1,713
Losses and temporary differences in year where no deferred tax asset recognised	(968)	(14)	(678)
Foreign profits taxed at other rates	486	100	(122)
UK tax rate change impact (1)	94	—	(338)
Non-deductible goodwill impairment	(124)	(28)	(49)
Items not allowed for tax			
- losses on disposal and write-downs	(15)	(19)	(19)
- UK bank levy	(50)	(54)	(47)
- regulatory and legal actions	(226)	(182)	(144)
- other disallowable items	(215)	(148)	(177)
Non-taxable items			
- gain on sale of WorldPay (Global Merchant Services)	—	—	37
- other non-taxable items	90	37	74
Taxable foreign exchange movements	(22)	(23)	12
Losses brought forward and utilised	102	218	—
(Reduction)/increase in carrying value of deferred tax asset in respect of:			
- UK losses	—	(850)	(701)
- US losses and temporary differences	—	(775)	—
- Ireland losses	—	153	—
Adjustments in respect of prior years (2)	239	69	132
Actual tax credit/(charge)	29	(2,033)	(307)

Notes:

(1) In recent years, the UK government has steadily reduced the rate of UK corporation tax, with the latest enacted rates standing at 20% with effect from 1 April 2015, 19% from 1 April 2017 and 18% from 1 April 2020. The Finance (No 2) Act 2015 restricts the rate at which tax losses are given credit in future periods to the main rate of UK corporation tax, excluding the Banking Surcharge 8% rate introduced by this Act. Deferred tax assets and liabilities at 31 December 2015 take into account the reduced rates in respect of tax losses and non-banking temporary differences and where appropriate, the banking surcharge inclusive rate in respect of other banking temporary differences.

(2) Prior year tax adjustments for 2015 include releases of tax provisions that reflect the reduction of exposures in countries where RBS is ceasing operations in line with the strategy to become a smaller, simpler UK focused bank. The prior year tax adjustments also reflects adjustments to reflect submitted tax computations in the UK and overseas and a further prior year tax credit in respect of tax losses arising in the Belfast Branch of Ulster Bank Ireland Limited reflecting UK tax law changes and European Court of Justice decisions on the surrender of tax losses.

7 Loss dealt with in the accounts of the Bank

As permitted by section 408(3) of the Companies Act 2006, no income statement for the Bank has been presented as a primary financial statement. Of the loss attributable to ordinary shareholders, £1,075 million loss (2014 - £2,119 million loss; 2013 - £1,257 million loss) has been dealt with in the accounts of the Bank.

8 Financial instruments - classification

The following tables show the Group's financial assets and liabilities in accordance with the categories of financial instruments in IAS 39. Assets and liabilities outside the scope of IAS 39 are shown within other assets and other liabilities.

	Group								
Assets	Held-for-trading £m	Designated as at fair value through profit or loss £m	Hedging derivatives £m	Available-for-sale £m	Loans and receivables £m	Held-to-maturity £m	Finance leases £m	Other assets £m	Total £m
Cash and balances at central banks	—	—		—	78,999	—			78,999
Loans and advances to banks									
- amounts due from fellow subsidiaries	886	—		—	671	—			1,557
- reverse repos	9,889	—		—	1,209	—			11,098
- other (1)	11,202	—		—	5,985	—			17,187
Loans and advances to customers									
- amounts due from holding company and fellow subsidiaries	—	—		—	1,258	—			1,258
- reverse repos	28,712	—		—	—	—			28,712
- other	17,516	63		—	283,709	—	3,699		304,987
Debt securities (2)	35,759	—		36,992	2,365	4,911			80,027
Equity shares	601	71		397	—	—			1,069
Settlement balances	—			—	4,108				4,108
Derivatives									
- amounts due from holding company and fellow subsidiaries	1,275		—						1,275
- other	258,258		3,550						261,808
Assets of disposal groups								3,486	3,486
Other assets	—	—		—	—	—		16,620	16,620
31 December 2015	364,098	134	3,550	37,389	378,304	4,911	3,699	20,106	812,191
Cash and balances at central banks	—	—		—	73,983	—			73,983
Loans and advances to banks									
- amounts due from fellow subsidiaries	672	—		—	1,661	—			2,333
- reverse repos	18,129	—		—	2,579	—			20,708
- other (1)	11,483	—		—	10,068	—			21,551
Loans and advances to customers									
- amounts due from holding company and fellow subsidiaries	—	—		—	1,323	—			1,323
- reverse repos	43,018	—		—	969	—			43,987
- other	22,830	61		—	304,619	—	4,118		331,628
Debt securities (2)	49,128	1		27,540	3,068	4,537			84,274
Equity shares	4,724	240		239	—	—			5,203
Settlement balances	—			—	4,710				4,710
Derivatives									
- amounts due from holding company and fellow subsidiaries	2,738		—						2,738
- other	346,677		5,167						351,844
Assets of disposal groups								81,033	81,033
Other assets*	—	—		—	—	—		20,067	20,067
31 December 2014	499,399	302	5,167	27,779	402,980	4,537	4,118	101,100	1,045,382

*Restated - refer to page 148 for further details.

For the notes to this table refer to page 178.

Liabilities	Held-for-trading £m	Designated as at fair value through profit or loss £m	Hedging derivatives £m	Amortised cost £m	Other liabilities £m	Total £m
	Group					
Deposits by banks						
- amounts due to fellow subsidiaries	190	—		3,809		3,999
- repos	9,657	—		609		10,266
- other (3)	20,285	—		7,544		27,829
Customer accounts						
- amounts due to holding company	—	—		5,021		5,021
- repos	25,570	—		1,542		27,112
- other (4)	11,723	2,661		327,557		341,941
Debt securities in issue (5)	3,881	5,873		16,050		25,804
Settlement balances	—	—		3,383		3,383
Short positions	20,808	—				20,808
Derivatives						
- amounts due to holding company and fellow subsidiaries	1,283	—	—			1,283
- other	251,693	—	2,572			254,265
Subordinated liabilities						
- amounts due to holding company	—	—		18,502		18,502
- other	—	327		8,201		8,528
Liabilities of disposal groups					2,980	2,980
Other liabilities	—	—		1,886	16,677	18,563
31 December 2015	345,090	8,861	2,572	394,104	19,657	770,284
Deposits by banks						
- amounts due to fellow subsidiaries	219	1		3,988		4,208
- repos	23,990	—		794		24,784
- other (3)	25,234	—		9,624		34,858
Customer accounts						
- amounts due to holding company	—	—		5,843		5,843
- repos	35,985	—		1,365		37,350
- other (4)	15,048	4,731		332,027		351,806
Debt securities in issue (5)	6,487	9,607		25,902		41,996
Settlement balances	—	—		4,498		4,498
Short positions	23,028	—				23,028
Derivatives						
- amounts due to holding company and fellow subsidiaries	2,005	—	—			2,005
- other	345,524	—	3,254			348,778
Subordinated liabilities						
- amounts due to holding company	—	—		19,639		19,639
- other	—	345		10,485		10,830
Liabilities of disposal groups					71,284	71,284
Other liabilities*	—	—		1,815	14,972	16,787
31 December 2014	477,520	14,684	3,254	415,980	86,256	997,694

*Restated - refer to page 148 for further details.

For the notes to this table refer to page 178.

The above includes amounts due from/to:

	Group			
	2015		2014	
	Holding company £m	Fellow subsidiaries £m	Holding company £m	Fellow subsidiaries £m
Assets				
Loans and advances to customers	895	363	938	385
Derivatives	65	1,210	30	2,708
Liabilities				
Derivatives	218	1,065	179	1,826

Notes:
(1) Includes items in the course of collection from other banks of £830 million (2014 - £980 million).
(2) Debt securities balances with Group companies are shown on pages 112 to 114.
(3) Includes items in the course of transmission to other banks of £338 million (2014 - £513 million).
(4) The carrying amount of other customer accounts designated as at fair value through profit or loss is £297 million (2014 - £432 million) higher than the principal amount. No amounts have been recognised in profit or loss for changes in credit risk associated with these liabilities as the changes are immaterial both during the period and cumulatively. Measured as the change in fair value from movements in the period in the credit risk premium payable.
(5) Comprises bonds and medium term notes of £24,860 million (2014 - £40,760 million) and certificates of deposit and other commercial paper of £944 million (2014 - £1,236 million).

Amounts included in operating (loss)/profit before tax:

	Group		
	2015 £m	2014 £m	2013 £m
Gains/(losses) on financial assets/liabilities designated as at fair value through profit or loss	285	43	(88)
Losses on disposal or settlement of loans and receivables	(551)	(236)	(137)

8 Financial instruments - classification continued

The following tables show the Bank's financial assets and financial liabilities in accordance with the categories of financial instruments in IAS 39. Assets and liabilities outside the scope of IAS 39 are shown within other assets and other liabilities.

	Bank								
Assets	Held-for-trading £m	Designated as at fair value through profit or loss £m	Hedging derivatives £m	Available-for-sale £m	Loans and receivables £m	Held-to-maturity £m	Finance leases £m	Other assets £m	Total £m
Cash and balances at central banks	—	—		—	76,904	—			76,904
Loans and advances to banks									
- amounts due from subsidiaries	3,838	—		—	20,253	—			24,091
- reverse repos	7,516	—		—	1,208	—			8,724
- other (1)	10,975	—		—	1,560	—			12,535
Loans and advances to customers									
- amounts due from holding company and subsidiaries	2,954	—		—	25,329	—			28,283
- reverse repos	18,187	—		—	—	—			18,187
- other	17,341	63		—	97,734	—	44		115,182
Debt securities (2)	30,811	—		35,220	5,660	4,911			76,602
Equity shares	599	—		332	—	—			931
Investment in Group undertakings	—	—		—	—	—		34,482	34,482
Settlement balances	—	—		—	3,053	—			3,053
Derivatives									
- amounts due from holding company and subsidiaries	4,726		—						4,726
- other	258,370		2,505						260,875
Other assets	—	—		—	—	—		4,607	4,607
31 December 2015	355,317	63	2,505	35,552	231,701	4,911	44	39,089	669,182
Cash and balances at central banks	—	—		—	70,952	—			70,952
Loans and advances to banks									
- amounts due from subsidiaries	2,172	—		—	22,667	—			24,839
- reverse repos	12,791	—		—	2,030	—			14,821
- other (1)	11,070	—		—	4,171	—			15,241
Loans and advances to customers									
- amounts due from holding company and subsidiaries	11,652	—		9	29,535	—			41,196
- reverse repos	30,976	—		—	969	—			31,945
- other	22,645	60		—	121,888	—	43		144,636
Debt securities (2)	39,210	—		24,725	19,122	4,537			87,594
Equity shares	4,714	40		126	—	—			4,880
Investment in Group undertakings	—	—		—	—	—		39,857	39,857
Settlement balances	—	—		—	3,381	—			3,381
Derivatives									
- amounts due from holding company and subsidiaries	9,268		—						9,268
- other	346,727		3,830						350,557
Other assets*	—	—		—	—	—		5,829	5,829
31 December 2014	491,225	100	3,830	24,860	274,715	4,537	43	45,686	844,996

*Restated - refer to page 148 for further details

For the notes to this table refer to page 181.

Liabilities	Bank					
	Held-for-trading £m	Designated as at fair value through profit or loss £m	Hedging derivatives £m	Amortised cost £m	Other liabilities £m	Total £m
Deposits by banks						
- amounts due to subsidiaries	1,924	—		114,419		116,343
- repos	6,180	—		610		6,790
- other (3)	20,253	—		3,834		24,087
Customer accounts						
- amounts due to holding company and subsidiaries	4,686	—		12,181		16,867
- repos	18,591	—		1,542		20,133
- other (4)	11,703	284		89,787		101,774
Debt securities in issue (5)	3,881	5,202		14,278		23,361
Settlement balances	—	—		2,363		2,363
Short positions	17,593	—				17,593
Derivatives						
- amounts due to holding company and subsidiaries	3,528		—			3,528
- other	252,000		1,844			253,844
Subordinated liabilities						
- amounts due to holding company	—	—	—	18,485		18,485
- other	—	327	—	6,722		7,049
Other liabilities	—	—		1,205	4,583	5,788
31 December 2015	340,339	5,813	1,844	265,426	4,583	618,005
Deposits by banks						
- amounts due to subsidiaries	3,567	9		117,913		121,489
- repos	21,254	—		794		22,048
- other (3)	24,824	—		6,094		30,918
Customer accounts						
- amounts due to holding company and subsidiaries	2,821	—		26,419		29,240
- repos	32,326	—		1,364		33,690
- other (4)	15,035	681		94,870		110,586
Debt securities in issue (5)	6,487	8,950		21,306		36,743
Settlement balances	—	—		3,098		3,098
Short positions	16,590	—				16,590
Derivatives						
- amounts due to holding company and subsidiaries	6,585		—			6,585
- other	346,079		2,083			348,162
Subordinated liabilities						
- amounts due to holding company	—	—		18,535		18,535
- other	—	345		8,600		8,945
Other liabilities*	—	—		1,143	4,671	5,814
31 December 2014	475,568	9,985	2,083	300,136	4,671	792,443

*Restated - refer to page 148 for further details

For the notes to this table refer to page 181.

The above includes amounts due from/to:

	Bank					
	2015			2014		
	Holding company £m	Fellow subsidiaries £m	Subsidiaries £m	Holding company £m	Fellow subsidiaries £m	Subsidiaries £m
Assets						
Loans and advances to banks	—	2,409	21,682	—	3,370	21,469
Loans and advances to customers	895	4	27,384	938	69	40,190
Derivatives	65	1,210	3,451	30	2,708	6,530
Liabilities						
Deposits by banks	—	11,496	104,847	—	12,452	109,037
Customer accounts	5,021	—	11,846	5,843	—	23,397
Derivatives	218	1,065	2,245	179	1,826	4,580

Notes:
(1) Includes items in the course of collection from other banks of £216 million (2014 - £237 million).
(2) Debt securities balances with Group companies are shown on pages 112 to 114.
(3) Includes items in the course of transmission to other banks of £192 million (2014 - £367 million).
(4) The carrying amount of other customer accounts designated as at fair value through profit or loss is £29 million (2014 - £54 million) higher than the principal amount. No amounts have been recognised in profit or loss for changes in credit risk associated with these liabilities as the changes are immaterial both during the period and cumulatively. Measured as the change in fair value from movements in the period in the credit risk premium payable.
(5) Comprises bonds and medium term notes of £22,418 million (2014 - £35,517 million) and certificates of deposit and other commercial paper of £943 million (2014 - £1,226 million).

The tables below present information on financial assets and liabilities that are offset on the balance sheet under IFRS or subject to enforceable master netting agreements only, together with financial collateral received or given.

	Offsetable instruments			Offsetable potential not recognised by IFRS			
2015	Gross £m	IFRS offset £m	Balance sheet £m	Effect of master netting agreements and similar arrangements £m	Cash collateral £m	Other financial collateral £m	Net amount after the effect of netting arrangements and related collateral £m
Assets							
Derivatives	381,673	(123,662)	258,011	(215,183)	(27,614)	(7,535)	7,679
Reverse repurchase agreements	74,171	(34,361)	39,810	(2,500)	—	(37,185)	125
Loans to customers	2,955	(2,955)	—	—	—	—	—
Settlement balances	1,271	(1,225)	46	(26)	—	—	20
	460,070	(162,203)	297,867	(217,709)	(27,614)	(44,720)	7,824
Liabilities							
Derivatives	369,416	(118,366)	251,050	(215,183)	(25,729)	(8,213)	1,925
Repurchase agreements	71,739	(34,361)	37,378	(2,500)	—	(34,878)	—
Customer accounts	8,251	(8,251)	—	—	—	—	—
Settlement balances	1,872	(1,225)	647	(26)	—	—	621
	451,278	(162,203)	289,075	(217,709)	(25,729)	(43,091)	2,546
2014							
Assets							
Derivatives	590,716	(245,418)	345,298	(296,156)	(32,629)	(7,005)	9,508
Reverse agreements	95,392	(30,822)	64,570	(5,016)	—	(59,505)	49
Loans to customers	2,921	(2,921)	—	—	—	—	—
Settlement balances	2,094	(1,997)	97	—	—	—	97
	691,123	(281,158)	409,965	(301,172)	(32,629)	(66,510)	9,654
Liabilities							
Derivatives	584,561	(241,235)	343,326	(296,156)	(30,015)	(14,433)	2,722
Repurchase agreements	91,887	(30,822)	61,065	(5,016)	—	(56,049)	—
Customer accounts	7,104	(7,104)	—	—	—	—	—
Settlement balances	1,998	(1,997)	1	—	—	—	1
	685,550	(281,158)	404,392	(301,172)	(30,015)	(70,482)	2,723

2015	Offsetable instruments			Offsetable potential not recognised by IFRS			
	Gross £m	IFRS offset £m	Balance sheet £m	Effect of master netting agreements and similar arrangements £m	Cash collateral £m	Other financial collateral £m	Net amount after the effect of netting arrangements and related collateral £m
Assets							
Derivatives	385,285	(123,662)	261,623	(216,601)	(27,595)	(7,464)	9,963
Reverse repurchase agreements	47,285	(20,374)	26,911	(2,051)	—	(24,860)	—
Loans to customers	2,955	(2,955)	—	—	—	—	—
Settlement balances	188	(168)	20	—	—	—	20
	435,713	(147,159)	288,554	(218,652)	(27,595)	(32,324)	9,983
Liabilities							
Derivatives	371,569	(118,366)	253,203	(216,601)	(25,729)	(8,212)	2,661
Repurchase agreements	47,297	(20,374)	26,923	(2,051)	—	(24,872)	—
Customer accounts	8,251	(8,251)	—	—	—	—	—
Settlement balances	193	(168)	25	—	—	—	25
	427,310	(147,159)	280,151	(218,652)	(25,729)	(33,084)	2,686
2014							
Assets							
Derivatives	595,932	(245,413)	350,519	(299,930)	(32,616)	(6,978)	10,995
Reverse repurchase agreements	61,651	(14,951)	46,700	(4,751)	—	(41,949)	—
Loans to customers	2,921	(2,921)	—	—	—	—	—
Settlement balances	228	(156)	72	—	—	—	72
	660,732	(263,441)	397,291	(304,681)	(32,616)	(48,927)	11,067
Liabilities							
Derivatives	588,399	(241,230)	347,169	(299,930)	(30,015)	(14,433)	2,791
Repurchase agreements	69,620	(14,951)	54,669	(4,751)	—	(49,918)	—
Customer accounts	7,104	(7,104)	—	—	—	—	—
Settlement balances	156	(156)	—	—	—	—	—
	665,279	(263,441)	401,838	(304,681)	(30,015)	(64,351)	2,791

8 Financial instruments - classification continued

Reclassification of financial instrument

There were no reclassifications in 2015. In 2008 and 2009, financial assets were reclassified from held-for-trading (HFT) into loans and receivables (LAR) and from HFT into available-for-sale (AFS). The tables below show the carrying value, fair value and the effect on profit or loss of these reclassifications.

	Group					
			Amount recognised in income statement		Amount that would have been recognised had reclassification not occurred	Reduction in profit or loss as a result of reclassification
2015	Carrying value £m	Fair value £m	Income £m	Impairment losses £m	£m	£m
Reclassified from HFT to LAR	1,002	877	(19)	(15)	4	38
Reclassified from HFT to AFS	21	21	—	—	2	2
	1,023	898	(19)	(15)	6	40
2014						
Reclassified from HFT to LAR	1,506	1,348	15	(76)	194	255
Reclassified from HFT to AFS	64	64	7	—	7	—
	1,570	1,412	22	(76)	201	255

The table below shows the carrying value and fair value of reclassifications undertaken by the Bank.

	Bank			
	2015		2014	
	Carrying value £m	Fair value £m	Carrying value £m	Fair value £m
Reclassified from HFT to LAR	1,002	877	1,331	1,177
Reclassified from HFT to AFS	21	21	64	64
	1,023	898	1,395	1,241

In 2014, the Group and the Bank reclassified UK Government bonds with a fair value of £3.6 billion from AFS to held-to-maturity (HTM).

9 Financial instruments - valuation

Valuation of financial instruments carried at fair value

Control environment

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

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

Independent price verification (IPV)

IPV is a key element of the control environment. Valuations are first performed by the business which entered into the transaction. Such valuations may be directly from available prices, or may be derived using a model and variable model inputs. These valuations are reviewed, and if necessary amended, by a team independent of those trading the financial instruments, in the light of available pricing evidence.

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

Governance framework

IPV takes place at least each month end date, for exposures in the regulatory trading book and at least quarterly for exposures in the regulatory banking book. The IPV control includes formalised reporting and escalation of any valuation differences in breach of established thresholds. The Pricing Unit determines IPV policy, monitors adherence to that policy and performs additional independent reviews of highly subjective valuation issues.

The Modelled Product Review Committee sets the policy for model documentation, testing and review, and prioritises models with significant exposure for review by the RBS Group Pricing Model Risk team. The CIB and RCR Valuation Committees are made up of valuation specialists and senior business representatives from various functions and oversee pricing, reserving and valuations issues. These committees meet monthly to review and ratify any methodology changes. The Executive Valuation Committee meets quarterly to address key material and subjective valuation issues, to review items escalated by the CIB and RCR Valuation Committees and to discuss other relevant matters including prudential valuation.

Valuation hierarchy

Initial classification of a financial instrument is carried out by the Product Control team following the principles in IFRS 13. They base their judgment on information gathered during the IPV process for instruments which include the sourcing of independent prices and model inputs. The quality and completeness of the information gathered in the IPV process gives an indication as to the liquidity and valuation uncertainty of an instrument.

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

Valuation techniques

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

Non-modelled products

Non-modelled products are valued directly from a price input typically on a position by position basis and include cash, equities and most debt securities.

Modelled products

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

Inputs to valuation models

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

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

Credit spreads - where available, these are derived from prices of credit default swaps or other credit based instruments, such as debt securities. For others, credit spreads are obtained from pricing services.

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

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

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

Commodity prices - many commodities are actively traded in spot and forward contracts and futures on exchanges in London, New York and other commercial centres.

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

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

Counterparty credit spreads - adjustments are made to market prices (or parameters) when the creditworthiness of the counterparty differs from that of the assumed counterparty in the market price (or parameters).

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

Consensus pricing

The Group uses consensus prices for the IPV of some instruments. The consensus service encompasses the equity, interest rate, currency, commodity, credit, property, fund and bond markets, providing comprehensive matrices of vanilla prices and a wide selection of exotic products. CIB and RCR contribute to consensus pricing services where there is a significant interest either from a positional point of view or to test models for future business use. Data sourced from consensus pricing services are used for a combination of control processes including direct price testing, evidence of observability and model testing. In practice this means that the Group submits prices for all material positions for which a service is available. Data from consensus services are subject to the same level of quality review as other inputs used for IPV process.

In order to determine a reliable fair value, where appropriate, management applies valuation adjustments to the pricing information gathered from the above sources. The sources of independent data are reviewed for quality and are applied in the IPV processes using a formalised input quality hierarchy. These adjustments reflect the Group's assessment of factors that market participants would consider in setting a price.

Furthermore, on an ongoing basis, the Group assesses the appropriateness of any model used. To the extent that the price determined by internal models does not represent the fair value of the instrument, for instance in highly stressed market conditions, the Group makes adjustments to the model valuation to calibrate to other available pricing sources.

Where unobservable inputs are used, the Group may determine a range of possible valuations derived from differing stress scenarios to determine the sensitivity associated with the valuation. When establishing the fair value of a financial instrument using a valuation technique, the Group considers adjustments to the modelled price which market participants would make when pricing that instrument. Such adjustments include the credit quality of the counterparty and adjustments to compensate for model limitations.

Valuation reserves

When valuing financial instruments in the trading book, adjustments are made to mid-market valuations to cover bid-offer spread, liquidity and credit risk. A breakdown of valuation adjustments is provided in Capital and risk management: Derivatives on page 118.

Credit valuation adjustments (CVA)

CVA represents an estimate of the adjustment to fair value that a market participant would make to incorporate the counterparty credit risk inherent in derivative exposures. CVA is actively managed by a credit and market risk hedging process, and therefore movements in CVA are partially offset by trading revenue on the hedges.

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

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

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

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

Bid-offer, liquidity and other reserves

Fair value positions are adjusted to bid (long positions) or offer (short positions) levels, by marking individual cash positions directly to bid or offer or by taking bid-offer reserves calculated on a portfolio basis for derivatives exposures. The bid-offer approach is based on current market spreads and standard market bucketing of risk.

Bid-offer adjustments for each risk factor (including delta (the degree to which the price of an instrument changes in response to a change in the price of the underlying), vega (the degree to which the price of an instrument changes in response to the volatility in the price of the underlying), correlation (the degree to which prices of different instruments move together)) are determined by aggregating similar risk exposures arising on different products. Additional basis bid-offer reserves are taken where these are charged in the market.

Bid-offer spreads vary by maturity and risk type to reflect different spreads in the market. For positions where there is no observable quote, the bid-offer spreads are widened in comparison to proxies to reflect reduced liquidity or observability. Bid-offer methodologies may also incorporate liquidity triggers whereby wider spreads are applied to risks above pre-defined thresholds.

As permitted by IFRS 13, netting is applied on a portfolio basis to reflect the value at which the Group believes it could exit the portfolio, rather than the sum of exit costs for each of the portfolio's individual trades. This is applied where the asset and liability positions are managed as a portfolio for risk and reporting purposes.

Vanilla risk on exotic products is typically reserved as part of the overall portfolio based calculation e.g. delta and vega risk on exotic products are included within the delta and vega bid-offer calculations.

Product related risks such as correlation risk, attract specific bid-offer reserves. Additional reserves are provided for exotic products to ensure overall reserves match market close-out costs. These market close-out costs inherently incorporate risk decay and cross-effects (taking into account how changes in one risk factor may affect other inputs rather than treating all risk factors independently) that are unlikely to be adequately reflected in a static hedge based on vanilla instruments. Where there is limited bid-offer information for a product, the pricing approach and risk management strategy are taken into account when assessing the reserve.

The discount rates applied to derivative cash flows in determining fair value reflect any underlying collateral agreements. Collateralised derivatives are generally discounted at the relevant OIS rates at an individual trade level. Uncollateralised derivatives are discounted with reference to funding levels by applying a funding spread over benchmark interest rates on a portfolio basis (funding valuation adjustment).

Funding valuation adjustment (FVA)

FVA represent an estimate of the adjustment to fair value that a market participant would make to incorporate funding costs and benefits that arise in relation to uncollateralised derivative exposures.

Funding levels are applied to estimated potential future exposures, the modelling of which is consistent with the approach used in the calculation of CVA. The counterparty contingent nature of the exposures is reflected in the calculation.

Amounts deferred on initial recognition

On initial recognition of financial assets and liabilities valued using valuation techniques incorporating information other than observable market data, any difference between the transaction price and that derived from the valuation technique is deferred. Such amounts are recognised in profit or loss over the life of the transaction; when market data becomes observable; or when the transaction matures or is closed out as appropriate. At 31 December 2015, net gains of £81 million (2014 - £86 million) were carried forward. During the year, net gains of £16 million (2014 - £40 million) were deferred and £21 million (2014 - £139 million) were recognised in the income statement.

Own credit

The Group takes into account the effect of its own credit standing when valuing financial liabilities recorded at fair value in accordance with IFRS. Own credit spread adjustments are made when valuing issued debt held at fair value, including issued structured notes, and derivatives. An own credit adjustment is applied to positions where it is believed that counterparties would consider the Group's creditworthiness when pricing trades.

For issued debt this adjustment is based on debt issuance spreads above average inter-bank rates (at a range of tenors). Secondary senior debt issuance spreads are used in the calculation of the own credit adjustment applied to senior debt.

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

The own credit adjustment does not alter cash flows, is not used for performance management, is disregarded for regulatory capital reporting processes and will reverse over time as the liabilities mature.

The reserve movement between periods will not equate to the reported profit or loss for own credit. The balance sheet reserves are stated by conversion of underlying currency balances at spot rates for each period whereas the income statement includes intra-period foreign exchange sell-offs.

The effect of change in credit spreads could reverse in future periods provided the liability is not repaid at a premium or a discount.

The cumulative own credit adjustment (OCA) recorded on securities held-for-trading (HFT), designated as at fair value through profit or loss (DFV) and derivative liabilities are set out below.

	Debt securities in issue (2)			Subordinated liabilities			
Cumulative own credit adjustment (1)	HFT £m	DFV £m	Total £m	DFV £m	Total £m	Derivatives £m	Total £m
2015	(118)	(29)	(147)	47	(100)	10	(90)
2014	(397)	(107)	(504)	53	(451)	8	(443)

Carrying values of underlying liabilities	£bn	£bn	£bn	£bn	£bn
2015	3.9	5.9	9.8	0.3	10.1
2014	6.5	9.6	16.1	0.3	16.4

Notes:
(1) Includes wholesale and retail note issuances.
(2) The reserve movement between periods will not equate to the reported profit or loss for own credit. The balance sheet reserve is stated by conversion of underlying currency balances at spot rates for each period, whereas the income statement includes intra-period foreign exchange sell-offs.

Valuation hierarchy

The following tables show financial instruments carried at fair value on the Group's balance sheet by valuation hierarchy - level 1, level 2 and level 3.

	2015						2014					
					Level 3 sensitivity (5)						Level 3 sensitivity (5)	
	Level 1 £bn	Level 2 £bn	Level 3 £bn	Total £bn	Favourable £m	Unfavourable (£m)	Level 1 £bn	Level 2 £bn	Level 3 £bn	Total £bn	Favourable £m	Unfavourable (£m)
Assets												
Loans and advances	—	67.9	0.3	68.2	50	(40.0)	—	95.6	0.6	96.2	30	(30.0)
Debt securities	60.3	11.6	0.9	72.8	30	(20.0)	55	20.5	1.2	76.7	50	(40.0)
- of which AFS	32.3	4.4	0.3	37.0	10	(10.0)	18.9	8.3	0.3	27.5	20	(10.0)
Equity shares	0.6	—	0.5	1.1	50	(30.0)	4.5	0.3	0.4	5.2	50	(50.0)
- of which AFS	—	—	0.4	0.4	40	(20.0)	—	—	0.2	0.2	30	(10.0)
Derivatives	—	261.1	2.0	263.1	380	(390.0)	—	351.5	3.0	354.5	290	(290.0)
	60.9	340.6	3.7	405.2	510	(480.0)	59.5	467.9	5.2	532.6	420	(410.0)
Proportion	15.0%	84.1%	0.9%	100.0%			11.2%	87.8%	1.0%	100.0%		
Liabilities												
Deposits	—	69.7	0.4	70.1	—	(10)	—	105	0.2	105.2	—	(10)
Debt securities in issue	—	9.3	0.5	9.8	30	—	—	14.9	1.2	16.1	30	(40)
Short positions	18.6	2.2	—	20.8	—	—	19.9	3.1	—	23	—	—
Derivatives	—	253.8	1.7	255.5	260	(270)	—	347.8	3.1	350.9	220	(240)
Subordinated liabilities	—	0.3	—	0.3	—	—	—	0.3	—	0.3	—	—
	18.6	335.3	2.6	356.5	290	(280)	19.9	471.1	4.5	495.5	250	(290)
Proportion	5.2%	94.1%	0.7%	100.0%			4.1%	95.0%	0.9%	100.0%		

Notes:

(1) Level 1: valued using unadjusted quoted prices in active markets, for identical financial instruments. Examples include G10 government securities, listed equity shares, certain exchange-traded derivatives and certain US agency securities.

Level 2: valued using techniques based significantly on observable market data. Instruments in this category are valued using:
(a) quoted prices for similar instruments or identical instruments in markets which are not considered to be active; or
(b) valuation techniques where all the inputs that have a significant effect on the valuations are directly or indirectly based on observable market data.

Level 2 instruments included non-G10 government securities, most government agency securities, investment-grade corporate bonds, certain mortgage products, including CLOs, most bank loans, repos and reverse repos, less liquid listed equities, state and municipal obligations, most notes issued, and certain money market securities and loan commitments and most OTC derivatives.

Level 3: instruments in this category have been valued using a valuation technique where at least one input which could have a significant effect on the instrument's valuation, is not based on observable market data. Level 3 instruments primarily include cash instruments which trade infrequently, certain syndicated and commercial mortgage loans, certain emerging markets instruments, unlisted equity shares, certain residual interests in securitisations, CDOs, other mortgage-backed products and less liquid debt securities, certain structured debt securities in issue, and OTC derivatives where valuation depends upon unobservable inputs such as certain credit and exotic derivatives. No gain or loss is recognised on the initial recognition of a financial instrument valued using a technique incorporating significant unobservable data.

(2) Transfers between levels are deemed to have occurred at the beginning of the quarter in which the instruments were transferred. There were no significant transfers between level 1 and level 2.

(3) For an analysis of derivatives by type of contract refer to Capital and risk management - Balance sheet analysis - derivatives.

(4) The determination of an instrument's level cannot be made at a global product level as a single product type can be in more than one level. For example, a single name corporate credit default swap could be in Level 2 or Level 3 depending on whether the reference counterparty's obligations are liquid or illiquid.

(5) Sensitivity represents the favourable and unfavourable effect on the income statement or the statement of comprehensive income due to reasonably possible changes to valuations using reasonably possible alternative inputs in RBS's valuation techniques or models. Level 3 sensitivities are calculated at a sub-portfolio level and hence these aggregated figures do not reflect the correlation between some of the sensitivities. In particular, for some portfolios, the sensitivities may be negatively correlated where a downward movement in one asset would produce an upward movement in another, but due to the additive presentation above, this correlation cannot be shown.

Valuation techniques

The table below shows a breakdown of valuation techniques and the ranges for those unobservable inputs used in valuation models and techniques that have a material impact on the valuation of Level 3 financial instruments. The table excludes unobservable inputs where the impact on valuation is less significant. Movements in the underlying input may have a favourable or unfavourable impact on the valuation depending on the particular terms of the contract and the exposure. For example an increase in the credit spread of a bond would be favourable for the issuer and unfavourable for the note holder. Whilst we indicate where we consider that there are significant relationships between the inputs, these inter-relationships will be affected by macro economic factors including interest rates, foreign exchange rates or equity index levels.

	Level 3 (£bn)				Range	
Financial instruments	Assets	Liabilities	Valuation technique	Unobservable inputs	Low	High
Loans and advances	0.3					
			DCF based on recoveries	Credit spreads (1)	869bps	7852bps
				Price (2)	0%	99%
Customer accounts		0.4				
			DCF based on recoveries	Credit spreads (1)	0bps	25bps
Debt securities	0.9					
			Price	Price (2)	0%	117%
Equity Shares	0.5					
			Fund valuation statement	Valuation (4)	90%	110%
			DCF based on recoveries	Recovery rates (3)	0%	30%
			Price	Price (2)	0	883pence
Derivatives	2.0	1.7				
Credit	0.2	0.2	DCF based on recoveries	Recovery rates (3)	0%	40%
				Credit speads (1)	12bps	384bps
Interest and foreign exchange contracts	1.8	1.5	Option pricing model	Correlation (5)	0%	99%
				Volatility (6)	16%	99%

Notes:
(1) Credit spreads and discount margins: credit spreads and margins express the return required over a benchmark rate or index to compensate for the credit risk associated with a cash instrument. A higher credit spread would indicate that the underlying instrument has more credit risk associated with it. Consequently, investors require a higher yield to compensate for the higher risk. The discount rate comprises credit spread or margin plus the benchmark rate; it is used to value future cash flows.
(2) Price and yield: there may be a range of prices used to value an instrument that may be a direct comparison of one instrument or portfolio with another or, movements in a more liquid instrument may be used to indicate the movement in the value of a less liquid instrument. The comparison may also be indirect in that adjustments are made to the price to reflect differences between the pricing source and the instrument being valued, for example different maturity, credit quality, seniority or expected pay-outs. Similarly to price, an instrument's yield may be compared with other instruments' yields either directly or indirectly.
(3) Recovery rate: reflects market expectations about the return of principal for a debt instrument or other obligations after a credit event or on liquidation. Recovery rates tend to move conversely to credit spreads.
(4) Valuation: for private equity investments, risk may be measured by beta, estimated by looking at past prices of similar stocks and from valuation statements where valuations are usually derived from earnings measures such as EBITDA.
(5) Correlation: measures the degree by which two prices or other variables are observed to move together. If they move in the same direction there is positive correlation; if they move in opposite directions there is negative correlation. Correlations typically include relationships between: default probabilities of assets in a basket (a group of separate assets), exchange rates, interest rates and other financial variables.
(6) Volatility: a measure of the tendency of a price to change with time.
(7) Level 3 structured notes issued of £0.5 billion are not included in the table above as valuation is consistent with the valuation of the embedded derivative component.
(8) The Group does not have any material liabilities measured at fair value that are issued with an inseparable third party credit enhancement.
(9) The table above excludes unobservable inputs where the impact on valuation is less significant. Movements in the underlying input may have a favourable or unfavourable impact on the valuation depending on the particular terms of the contract and the exposure. For example, an increase in the credit spread of a bond would be favourable for the issuer but unfavourable for the note holder. Whilst the Group indicates where it considers that there are significant relationships between the inputs, their inter-relationships will be affected by macro economic factors including interest rates, foreign exchange rates or equity index levels.

The Level 3 sensitivities on the previous page are calculated at a trade or low level portfolio basis. They are not calculated on an overall portfolio basis and therefore do not reflect the likely potential uncertainty on the portfolio as a whole. The figures are aggregated and do not reflect the correlated nature of some of the sensitivities. In particular, for some of the portfolios the sensitivities may be negatively correlated where a downwards movement in one asset would produce an upwards movement in another, but due to the additive presentation of the above figures this correlation cannot be displayed. The actual potential downside sensitivity of the total portfolio may be less than the non-correlated sum of the additive figures as shown in the above table.

Judgmental issues

The diverse range of products traded by the Group results in a wide range of instruments that are classified into Level 3 of the hierarchy. Whilst the majority of these instruments naturally fall into a particular level, for some products an element of judgment is required. The majority of RBS's financial instruments carried at fair value are classified as Level 2: inputs are observable either directly (i.e. as a price) or indirectly (i.e. derived from prices).

Active and inactive markets

A key input in the decision making process for the allocation of assets to a particular level is liquidity. In general, the degree of valuation uncertainty depends on the degree of liquidity of an input.

Where markets are liquid or very liquid, little judgment is required. However, when the information regarding the liquidity in a particular market is not clear, a judgment may need to be made. This can be more difficult as assessing the liquidity of a market is not always straightforward. For an equity traded on an exchange, daily volumes of trading can be seen, but for an over-the-counter (OTC) derivative assessing the liquidity of the market with no central exchange is more difficult.

A key related issue is where a market moves from liquid to illiquid or vice versa. Where this change is considered to be temporary, the classification is not changed. For example, if there is little market trading in a product on a reporting date but at the previous reporting date and during the intervening period the market has been considered to be liquid, the instrument will continue to be classified in the same level in the hierarchy. This is to provide consistency so that transfers between levels are driven by genuine changes in market liquidity and do not reflect short term or seasonal effects.

The breadth and depth of the IPV data allows for a rules based quality assessment to be made of market activity, liquidity and pricing uncertainty, which assists with the process of allocation to an appropriate level. Where suitable independent pricing information is not readily available, the quality assessment will result in the instrument being assessed as Level 3.

Modelled products

For modelled products the market convention is to quote these trades through the model inputs or parameters as opposed to a cash price equivalent. A mark-to-market is derived from the use of the independent market inputs calculated using RBS's model.

The decision to classify a modelled instrument as Level 2 or 3 will be dependent upon the product/model combination, the currency, the maturity, the observability and quality of input parameters and other factors. All these must be assessed to classify the asset.

If an input fails the observability or quality tests then the instrument is considered to be in Level 3 unless the input can be shown to have an insignificant effect on the overall valuation of the product.

The majority of derivative instruments for example vanilla interest rate swaps, foreign exchange swaps and liquid single name credit derivatives are classified as Level 2 as they are vanilla products valued using observable inputs. The valuation uncertainty on these is considered to be low and both input and output testing may be available.

Non-modelled products

Non-modelled products are generally quoted on a price basis and can therefore be considered for each of the three levels. This is determined by the market activity, liquidity and valuation uncertainty of the instruments which is in turn measured from the availability of independent data used by the IPV process to allocate positions to IPV quality levels.

The availability and quality of independent pricing information are considered during the classification process. An assessment is made regarding the quality of the independent information. For example, where consensus prices are used for non-modelled products, a key assessment of the quality of a price is the depth of the number of prices used to provide the consensus price. If the depth of contributors falls below a set hurdle rate, the instrument is considered to be Level 3. This hurdle rate is that used in the IPV process to determine the IPV quality rating. However, where an instrument is generally considered to be illiquid, but regular quotes from market participants exist, these instruments may be classified as Level 2 depending on frequency of quotes, other available pricing and whether the quotes are used as part of the IPV process or not.

For some instruments with a wide number of available price sources, there may be differing quality of available information and there may be a wide range of prices from different sources. In these situations the highest quality source is used to determine the classification of the asset. For example, a tradable quote would be considered a better source than a consensus price.

Level 3 portfolios and sensitively methodologies

Reasonably possible alternative assumptions of unobservable inputs are determined based on a 90% confidence interval. The assessments recognise different favourable and unfavourable valuation movements where appropriate. Each unobservable input within a product is considered separately and sensitivity is reported on an additive basis.

Alternative assumptions are determined with reference to all available evidence including consideration of the following: quality of independent pricing information taking into account consistency between different sources, variation over time, perceived tradability or otherwise of available quotes; consensus service dispersion ranges; volume of trading activity and market bias (e.g. one-way inventory); day 1 profit or loss arising on new trades; number and nature of market participants; market conditions; modelling consistency in the market; size and nature of risk; length of holding of position; and market intelligence.

Other considerations

Valuation adjustments

CVA applied to derivative exposures and own credit adjustments applied to derivative liabilities are calculated on a portfolio basis. Whilst the methodology used to calculate each of these adjustments references certain inputs which are not based on observable market data, the uncertainty of the inputs is not considered to have a significant effect on the net valuation of the related portfolios. The classification of the derivative portfolios which the valuation adjustments are applied to is not determined by the observability of the valuation adjustments, and any related sensitivity does not form part of the Level 3 sensitivities presented.

Funding related adjustments

The discount rates applied to derivative cash flows in determining fair value reflect any underlying collateral agreements. Collateralised derivative exposures are generally discounted at the relevant OIS rates whilst funding valuation adjustments are applied to uncollateralised derivative exposures. Whilst these adjustments reference certain inputs which are not based on observable market data, the uncertainty of the inputs is not considered to have a significant effect on the valuation of the individual trades. The classification of derivatives is not determined by the observability of these adjustments, and any related sensitivity does not form part of the Level 3 sensitivities presented.

Own credit - issued debt

For issued debt the own credit adjustment is based on debt issuance spreads above average inter-bank rates at the reporting date (at a range of tenors). Whilst certain debt issuance spreads are not based on observable market data, the uncertainty of the inputs is not considered to have a significant effect on the valuation of individual trades. Neither the classification of issued debt nor any related valuation sensitivities are determined by the observability of the debt issuance spreads.

Movement in Level 3

	2015				2014			
	FVTPL assets (2)	AFS assets	Total assets	Total liabilities	FVTPL assets (2)	AFS assets	Total assets	Total liabilities
	£m	£m	£m	£m	£m	£m	£m	£m
At 1 January	4,584	512	5,096	4,537	5,183	1,380	6,563	4,575
Amount recorded in the income statement (1)	(961)	—	(961)	(1,163)	98	4	102	51
Amount recorded in the statement of comprehensive income	—	194	194	—	—	(48)	(48)	—
Level 3 transfers in	1,628	150	1,778	1,439	1,088	6	1,094	1,744
Level 3 transfers out	(655)	(34)	(689)	(682)	(967)	(107)	(1,074)	(698)
Issuances	1	—	1	36	—	—	—	109
Purchases	557	7	564	40	858	7	865	59
Settlements	(868)	(117)	(985)	(1,573)	(981)	(367)	(1,348)	(1,257)
Sales	(1,288)	(31)	(1,319)	(15)	(622)	(373)	(995)	(50)
Foreign exchange and other adjustments	10	1	11	3	8	10	18	16
At 31 December	3,008	682	3,690	2,622	4,665	512	5,177	4,549
Amounts recorded in the income statement in respect of balances held at year end								
- unrealised	(156)	3	(153)	(470)	57	3	60	(56)
- realised	(43)	12	(31)	(4)	(83)	3	(80)	105

Notes:
(1) Net gains on HFT instruments of £22 million (2014 - net losses of £123 million) were recorded in income from trading activities in continuing operations. Net gains on other instruments of £180 million (2014 - £174 million) were recorded in other operating income and interest income as appropriate in continuing operations. There were no losses (2014 - nil) in discontinued operations.
(2) Fair value through profit or loss comprises held-for-trading predominantly and designated at fair value through profit of loss.

Fair value of financial instruments not carried at fair value

The following table shows the carrying value and fair value of financial instruments carried at amortised cost on the balance sheet.

	Group						Bank					
	Items where fair value approximates carrying value	Carrying value	Fair value	Fair value hierarchy level			Items where fair value approximates carrying value	Carrying value	Fair value	Fair value hierarchy level		
2015	£bn	£bn	£bn	Level 1 £bn	Level 2 £bn	Level 3 £bn	£bn	£bn	£bn	Level 1 £bn	Level 2 £bn	Level 3 £bn
Financial assets												
Cash and balances at central banks	79.0						76.9					
Loans and advances to banks	0.8	7.0	7.0	—	3.5	3.5	0.2	22.8	23.0	—	7.4	15.6
Loans and advances to customers		288.7	281.9	—	1.3	280.6		123.1	119.6	—	19.9	99.7
Debt securities		7.3	7.2	5.0	1.0	1.2		10.6	10.5	5.0	2.9	2.6
Settlement balances	4.1						3.1					
Financial liabilities												
Deposits by banks	4.7	7.3	7.3	—	4.0	3.3	47.6	71.2	71.4	—	23.1	48.3
Customer accounts	253.9	80.2	80.2	—	31.1	49.1	65.2	38.3	38.6	—	13.2	25.4
Debt securities in issue		16.0	16.7	—	14.4	2.3		14.3	15.2	—	14.1	1.1
Settlement balances	3.4						2.4					
Notes in circulation (1)	1.9						1.2					
Subordinated liabilities		26.7	27.7	—	16.4	11.3		25.2	26.4	—	15.2	11.2

	Group						Bank					
	Items where fair value approximates carrying value	Carrying value	Fair value	Fair value hierarchy level			Items where fair value approximates carrying value	Carrying value	Fair value	Fair value hierarchy level		
2014	£bn	£bn	£bn	Level 1 £bn	Level 2 £bn	Level 3 £bn	£bn	£bn	£bn	Level 1 £bn	Level 2 £bn	Level 3 £bn
Financial assets												
Cash and balances at central banks	74.0						71.0					
Loans and advances to banks	1.0	13.3	13.3	—	6.6	6.7	0.2	28.7	29.1	—	12.8	16.3
Loans and advances to customers		311.0	302.5	—	3.3	299.2		152.4	149.5	—	24.9	124.6
Debt securities		7.6	7.5	4.7	1.9	0.9		23.7	23.3	4.7	13.0	5.6
Settlement balances	4.7						3.4					
Financial liabilities												
Deposits by banks	4.6	9.8	9.8	—	3.1	6.7	5.2	119.6	120.2	—	28.0	92.2
Customer accounts	234.9	104.3	104.3	—	54.8	49.5	68.3	54.4	54.5	—	18.6	35.9
Debt securities in issue		25.9	27.2	—	24.2	3.0		21.3	22.7	—	21.3	1.4
Settlement balances	4.5						3.1					
Notes in circulation (1)	1.8						1.1					
Subordinated liabilities		30.1	31.7	—	19.8	11.9		27.1	28.8	—	17.1	11.7

Note:
(1) Included in provisions, accruals and other liabilities.

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

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

Short-term financial instruments

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

Loans and advances to banks and customers

In estimating the fair value of loans and advances to banks and customers measured at amortised cost, RBS's loans are segregated into appropriate portfolios reflecting the characteristics of the constituent loans. Two principal methods are used to estimate fair value:

(a) Contractual cash flows are discounted using a market discount rate that incorporates the current spread for the borrower or where this is not observable, the spread for borrowers of a similar credit standing. This method is used for portfolios where counterparties have external ratings: institutional and corporate lending in CIB.

(b) Expected cash flows (unadjusted for credit losses) are discounted at the current offer rate for the same or similar products. This approach is adopted for lending portfolios in UK PBB, Ulster Bank RoI Commercial Banking (SME loans) and Private Banking in order to reflect the homogeneous nature of these portfolios.

For certain portfolios where there are very few or no recent transactions, such as Ulster Bank RoI's portfolio of lifetime tracker mortgages, a bespoke approach is used based on available market data.

Debt securities

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

Deposits by banks and customer accounts

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

Debt securities in issue and subordinated liabilities

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

10 Financial instruments - maturity analysis

Remaining maturity

The following table shows the residual maturity of financial instruments, based on contractual date of maturity.

	Group					
	2015			2014		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central banks	78,999	—	78,999	73,983	—	73,983
Loans and advances to banks	29,649	193	29,842	43,741	851	44,592
Loans and advances to customers	112,136	222,821	334,957	147,673	229,265	376,938
Debt securities	27,318	52,709	80,027	23,866	60,408	84,274
Equity shares	—	1,069	1,069	—	5,203	5,203
Settlement balances	4,108	—	4,108	4,710	—	4,710
Derivatives	41,625	221,458	263,083	67,151	287,431	354,582
Liabilities						
Deposits by banks	41,558	536	42,094	62,039	1,811	63,850
Customer accounts	368,386	5,688	374,074	387,477	7,522	394,999
Debt securities in issue	7,913	17,891	25,804	8,093	33,903	41,996
Settlement balances and short positions	6,186	18,005	24,191	6,420	21,106	27,526
Derivatives	42,856	212,692	255,548	69,090	281,693	350,783
Subordinated liabilities	322	26,708	27,030	2,561	27,908	30,469

	Bank					
	2015			2014		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central banks	76,904	—	76,904	70,952	—	70,952
Loans and advances to banks	35,011	10,339	45,350	43,423	11,478	54,901
Loans and advances to customers	76,278	85,374	161,652	114,765	103,012	217,777
Debt securities	24,806	51,796	76,602	26,250	61,344	87,594
Equity shares	—	931	931	—	4,880	4,880
Settlement balances	3,053	—	3,053	3,381	—	3,381
Derivatives	41,950	223,651	265,601	68,447	291,378	359,825
Liabilities						
Deposits by banks	128,250	18,970	147,220	151,740	22,715	174,455
Customer accounts	131,342	7,432	138,774	157,548	15,968	173,516
Debt securities in issue	7,908	15,453	23,361	8,028	28,715	36,743
Settlement balances and short positions	4,476	15,480	19,956	4,462	15,226	19,688
Derivatives	43,015	214,357	257,372	70,454	284,293	354,747
Subordinated liabilities	307	25,227	25,534	2,133	25,347	27,480

On balance sheet liabilities

The tables below show the timing of cash outflows to settle financial liabilities, prepared on the following basis:

Financial liabilities are included at the earliest date on which the counterparty can require repayment regardless of whether or not such early repayment results in a penalty. If repayment is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the liability is included at the earliest possible date that the conditions could be fulfilled without considering the probability of the conditions being met. For example, if a structured note automatically prepays when an equity index exceeds a certain level, the cash outflow will be included in the less than three months' period whatever the level of the index at the year end. The settlement date of debt securities issued by certain securitisation vehicles consolidated by the Group depends on when cash flows are received from the securitised assets. Where these assets are prepayable, the timing of the cash outflow relating to securities assumes that each asset will be prepaid at the earliest possible date.

Liabilities with a contractual maturity of greater than 20 years - the principal amounts of financial liabilities that are repayable after 20 years or where the counterparty has no right to repayment of the principal, are excluded from the table along with interest payments after 20 years.

Held-for-trading liabilities - held-for-trading liabilities of £345.1 billion (2014 - £477.5 billion) for the Group and £340.3 billion (2014 - £475.6 billion) for the Bank, have been excluded from the tables.

	Group					
2015	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Deposits by banks	10,758	781	1	1	232	194
Customers accounts	328,245	6,360	1,744	322	8	22
Debt securities in issue	3,568	3,112	5,126	6,153	4,435	332
Derivatives held for hedging	142	271	597	408	632	701
Subordinated liabilities	478	1,089	5,353	7,587	11,956	6,011
Settlement balances and other liabilities	5,269	—	—	—	—	—
	348,460	11,613	12,821	14,471	17,263	7,260
Guarantees and commitments - notional amount						
Guarantees (1)	5,894	—	—	—	—	—
Commitments (2)	131,906	—	—	—	—	—
	137,800	—	—	—	—	—
2014						
Deposits by banks	12,076	784	793	8	575	140
Customers accounts	330,808	8,985	3,076	1,084	85	18
Debt securities in issue	1,889	5,375	9,958	5,511	8,884	1,924
Derivatives held for hedging	134	316	721	491	847	894
Subordinated liabilities	1,105	2,792	3,935	9,688	13,656	5,765
Settlement balances and other liabilities	6,305	5	3	—	—	—
	352,317	18,257	18,486	16,782	24,047	8,741
Guarantees and commitments - notional amount						
Guarantees (1,2)	10,973	—	—	—	—	—
Commitments (3)	212,335	—	—	—	—	—
	223,308	—	—	—	—	—

Notes:

(1) The Group is only called upon to satisfy a guarantee when the guaranteed party fails to meet its obligations. The Group expects most guarantees it provides to expire unused.

(2) Guarantees exclude the Asset Protection Scheme related financial guarantee contract of £680 million (2014 - £721 million) between the Bank and a fellow subsidiary.

(3) The Group has given commitments to provide funds to customers under undrawn formal facilities, credit lines and other commitments to lend subject to certain conditions being met by the counterparty. The Group does not expect all facilities to be drawn, and some may lapse before drawdown.

10 Financial instruments - maturity analysis continued

	Bank					
2015	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Deposits by banks	97,019	3,794	6,212	5,842	5,034	2,819
Customers accounts	94,519	3,319	1,502	1,606	2,040	1,275
Debt securities in issue	3,532	3,013	4,611	5,978	3,192	231
Derivatives held for hedging	111	212	458	298	428	483
Subordinated liabilities	453	1,032	5,226	7,453	11,418	5,547
Settlement balances and other liabilities	3,568	—	—	—	—	—
	199,202	11,370	18,009	21,177	22,112	10,355
Guarantees and commitments - notional amount						
Guarantees (1)	4,534	—	—	—	—	—
Commitments (2)	83,737	—	—	—	—	—
	88,271	—	—	—	—	—
2014						
Deposits by banks	98,112	6,505	6,365	5,326	2,184	8,884
Customers accounts	101,176	8,447	4,054	3,026	4,795	4,400
Debt securities in issue	1,804	5,229	9,525	5,218	8,414	1,467
Derivatives held for hedging	90	204	477	318	539	582
Subordinated liabilities	950	2,363	3,715	9,460	11,834	5,347
Settlement balances and other liabilities	4,241	—	—	—	—	—
	206,373	22,748	24,136	23,348	27,766	20,680
Guarantees and commitments - notional amount						
Guarantees (1,2)	7,678	—	—	—	—	—
Commitments (2)	126,759	—	—	—	—	—
	134,437	—	—	—	—	—

Notes:

(1) The Bank is only called upon to satisfy a guarantee when the guaranteed party fails to meet its obligations. The Bank expects most guarantees it provides to expire unused.

(2) Guarantees exclude the Asset Protection Scheme related financial guarantee contract of £680 million (2014 - £721 million) between the Bank and a fellow subsidiary.

(3) The Bank has given commitments to provide funds to customers under undrawn formal facilities, credit lines and other commitments to lend subject to certain conditions being met by the counterparty. The Bank does not expect all facilities to be drawn, and some may lapse before drawdown.

11 Financial assets - impairments

The following tables show the movement in the provision for impairment losses on loans and advances.

	Group				
	Individually assessed £m	Collectively assessed £m	Latent £m	2015 £m	2014 £m
At 1 January	11,207	5,190	1,007	17,404	25,045
Transfers to disposal groups	(20)	—	—	(20)	(553)
Currency translation and other adjustments	(443)	(110)	(23)	(576)	(657)
Amounts written-off	(7,788)	(1,162)	—	(8,950)	(5,253)
Recoveries of amounts previously written-off	101	71	—	172	201
(Releases)/losses to the income statement					
- continuing operations	(397)	(35)	(402)	(834)	(1,326)
- discontinued operations	—	—	—	—	194
Unwind of discount (recognised in interest income)	(51)	(93)	—	(144)	(247)
At 31 December (1)	2,609	3,861	582	7,052	17,404

	Bank				
	Individually assessed £m	Collectively assessed £m	Latent £m	2015 £m	2014 £m
At 1 January	2,337	808	319	3,464	6,236
Transfers to disposal groups	—	—	—	—	(17)
Currency translation and other adjustments	(57)	7	(2)	(52)	(65)
Disposals	(48)	—	—	(48)	—
Amounts written-off	(1,474)	(252)	—	(1,726)	(2,608)
Recoveries of amounts previously written-off	217	17	—	234	41
(Releases)losses to the income statement					
- continuing operations	(77)	8	(184)	(253)	(36)
Unwind of discount (recognised in interest income)	(26)	(21)	—	(47)	(87)
At 31 December (1)	872	567	133	1,572	3,464

Notes:
(1) Includes £1 million relating to loans and advances to banks (2014 - £40 million).
(2) The table above excludes impairments relating to securities.

	Group		
Impairment (releases)/losses charged to the income statement	2015 £m	2014 £m	2013 £m
Loans and advances to customers	(830)	(1,316)	8,173
Loans and advances to banks	(4)	(10)	(15)
	(834)	(1,326)	8,158
Debt securities	(3)	(11)	(21)
(Release)/losses charged to the income statement for continuing operations	(837)	(1,337)	8,137

	Group		
	2015 £m	2014 £m	2013 £m
Gross income not recognised but which would have been recognised under the original terms of the impaired loans			
UK	311	404	570
Overseas	124	141	562
	435	545	1,132
Interest on impaired loans included in net interest income			
UK	98	146	196
Overseas	46	101	194
	144	247	390

The following tables analyse impaired financial assets.

	Group					
	2015			2014		
	Cost £m	Provision £m	Carrying value £m	Cost £m	Provision £m	Carrying value £m
Loans and receivables						
Loans and advances to banks (1)	1	1	—	42	40	2
Loans and advances to customers (2)	10,748	6,469	4,279	25,040	16,357	8,683
	10,749	6,470	4,279	25,082	16,397	8,685

	Group	
	Carrying value 2015 £m	Carrying value 2014 £m
Available-for-sale securities		
Debt securities	9	143
Equity shares	31	22
Loans and receivables		
Debt securities	2	7
	42	172

	Bank					
	2015			2014		
	Cost £m	Provision £m	Carrying value £m	Cost £m	Provision £m	Carrying value £m
Loans and receivables						
Loans and advances to banks (1)	1	1	—	42	40	2
Loans and advances to customers (3)	2,807	1,437	1,370	6,135	3,105	3,030
	2,808	1,438	1,370	6,177	3,145	3,032

Notes:
(1) Impairment provisions individually assessed.
(2) Impairment provisions individually assessed on balances of £4,408 million (2014 - £16,590 million).
(3) Impairment provisions individually assessed on balances of £1,999 million (2014 - £4,963 million).

	Bank	
	Carrying value 2015 £m	Carrying value 2014 £m
Available-for-sale securities		
Debt securities	9	142
Equity shares	21	9
Loans and receivables		
Debt securities	2	7
	32	158

Financial and non-financial assets recognised on the balance sheet, obtained during the year by taking possession of collateral or calling on other credit enhancements, were £34 million (2014 - £43 million) for the Group and £11 million (2014 - £13 million) for the bank.

In general, the Group seeks to dispose of property and other assets not readily convertible into cash, obtained by taking possession of collateral, as rapidly as the market for the individual asset permits.

12 Derivatives

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

The Group enters into fair value hedges, cash flow hedges and hedges of net investments in foreign operations. The majority of the Group's interest rate hedges relate to the management of the Group's non-trading interest rate risk. The Group manages this risk within approved limits. Residual risk positions are hedged with derivatives principally interest rate swaps. Suitable larger financial instruments are fair value hedged; the remaining exposure, where possible, is hedged by derivatives documented as cash flow hedges and qualifying for hedge accounting. The majority of the Group's fair value hedges involve interest rate swaps hedging the interest rate risk in recognised financial assets and financial liabilities. Cash flow hedges relate to exposures to the variability in future interest payments and receipts on forecast transactions and on recognised financial assets and financial liabilities. The Group hedges its net investments in foreign operations with currency borrowings and forward foreign exchange contracts.

For cash flow hedge relationships of interest rate risk, the hedged items are actual and forecast variable interest rate cash flows arising from financial assets and financial liabilities with interest rates linked to LIBOR, EURIBOR or the Bank of England Official Bank Rate. The financial assets are customer loans and the financial liabilities are customer deposits and LIBOR linked medium-term notes and other issued securities. At 31 December 2015, variable rate financial assets of £77 billion (2014 - £80 billion) for the Group and £43 billion (2014 - £49 billion) for the Bank, and variable rate financial liabilities of £29 billion (2014 - £14 billion) for the Group and £21 billion (2014 - £6 billion) for the Bank were hedged in such cash flow hedge relationships.

For cash flow hedging relationships, the initial and ongoing prospective effectiveness is assessed by comparing movements in the fair value of the expected highly probable forecast interest cash flows with movements in the fair value of the expected changes in cash flows from the hedging interest rate swap. Prospective effectiveness is measured on a cumulative basis i.e. over the entire life of the hedge relationship. The method of calculating hedge ineffectiveness is the hypothetical derivative method. Retrospective effectiveness is assessed by comparing the actual movements in the fair value of the cash flows and actual movements in the fair value of the hedged cash flows from the interest rate swap over the life to date of the hedging relationship.

For fair value hedge relationships of interest rate risk, the hedged items are typically government bonds, large corporate fixed rate loans, fixed rate finance leases, fixed rate medium-term notes or preference shares classified as debt. At 31 December 2015, fixed rate financial assets of £25 billion (2014 - £17 billion) for the Group and £22 billion (2014 - £14 billion) for the Bank, and fixed rate financial liabilities of £16 billion (2014 - £25 billion) for the Group and £16 billion (2014 - £24 billion) for the Bank were hedged by interest rate swaps in fair value hedge relationships.

The initial and ongoing prospective effectiveness of fair value hedge relationships is assessed on a cumulative basis by comparing movements in the fair value of the hedged item attributable to the hedged risk with changes in the fair value of the hedging interest rate swap. Retrospective effectiveness is assessed by comparing the actual movements in the fair value of the hedged items attributable to the hedged risk with actual movements in the fair value of the hedging derivative over the life to date of the hedging relationship.

The following table shows the notional amounts and fair values of the Group's derivatives.

	Group					
	2015			2014		
	Notional amount £bn	Assets £m	Liabilities £m	Notional amount £bn	Assets £m	Liabilities £m
Exchange rate contracts						
Spot, forwards and futures	1,965	22,908	22,407	2,013	32,912	33,361
Currency swaps	762	18,372	21,813	860	22,297	26,776
Options purchased	484	13,706	—	896	23,456	—
Options written	495	—	13,943	881	—	23,451
Interest rate contracts						
Interest rate swaps	12,541	174,884	162,784	20,164	220,328	212,195
Options purchased	1,373	31,309	—	1,471	49,248	—
Options written	1,334	—	32,526	1,552	—	47,909
Futures and forwards	4,543	390	317	4,133	886	739
Credit derivatives	66	909	844	125	2,248	2,612
Equity and commodity contracts	18	605	914	79	3,207	3,740
		263,083	255,548		354,582	350,783

	Group			
	2015		2014	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Amounts above include:				
Due from/to holding company	65	218	30	179
Due from/to fellow subsidiaries	1,210	1,065	2,708	1,826

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

	Group			
	2015		2014	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Fair value hedging				
Interest rate contracts	1,261	1,647	1,870	1,962
Cash flow hedging				
Interest rate contracts	2,231	917	3,240	1,291
Exchange rate contracts	11	—	—	—
Net investment hedging				
Exchange rate contracts	47	8	57	1

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

	2015 £m	2014 £m
Fair value hedging		
Gains on the hedged items attributable to the hedged risk	143	644
Losses on the hedging instruments	(81)	(682)
Fair value hedging ineffectiveness	62	(38)
Cash flow hedging ineffectiveness	(23)	(33)
	39	(71)

The following table shows when hedged cash flows are expected to occur and when they will affect income for designated cash flow hedges.

	Group					
2015	0-1 years £m	1-5 years £m	5-10 years £m	10-20 years £m	Over 20 years £m	Total £m
Hedged forecast cash flows expected to occur						
Forecast receivable cash flows	332	828	231	—	—	1,391
Forecast payable cash flows	(119)	(192)	(62)	(78)	(11)	(462)
2014						
Hedged forecast cash flows expected to occur						
Forecast receivable cash flows	278	844	227	—	—	1,349
Forecast payable cash flows	(49)	(100)	(61)	(92)	(12)	(314)

	Bank					
	2015			2014		
	Notional amount £bn	Assets £m	Liabilities £m	Notional amount £bn	Assets £m	Liabilities £m
Exchange rate contracts						
Spot, forwards and futures	1,973	23,015	22,492	2,064	34,189	34,670
Currency swaps	768	18,880	21,835	868	22,616	26,725
Options purchased	484	13,669	—	897	23,474	—
Options written	495	—	13,933	882	—	23,469
Interest rate contracts						
Interest rate swaps	12,624	176,812	164,456	20,269	223,893	214,793
Options purchased	1,375	31,282	—	1,459	49,281	—
Options written	1,335	—	32,536	1,530	—	47,930
Futures and forwards	4,540	390	317	4,124	881	739
Credit derivatives	66	909	844	125	2,262	2,612
Equity and commodity contracts	20	644	959	80	3,229	3,809
		265,601	257,372		359,825	354,747

	Bank			
	2015		2014	
Amounts above include:	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Due from/to holding company	65	218	30	179
Due from/to fellow subsidiaries	1,210	1,065	2,708	1,826
Due from/to subsidiaries	3,451	2,245	6,530	4,580

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

	Bank			
	2015		2014	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Fair value hedging				
Exchange rate contracts	13	1	26	—
Interest rate contracts	1,197	1,198	1,797	1,338
Cash flow hedging				
Interest rate contracts	1,278	644	2,005	744
Exchange rate contracts	11	—	—	—
Net investment hedging				
Exchange rate contracts	6	1	2	1

The following table shows when hedged cash flows are expected to occur and when they will affect income for designated cash flow hedges.

	Bank					
2015	0-1 years £m	1-5 years £m	5-10 years £m	10-20 years £m	Over 20 years £m	Total £m
Hedged forecast cash flows expected to occur						
Forecast receivable cash flows	183	421	98	—	—	702
Forecast payable cash flows	(86)	(166)	(49)	(57)	(2)	(360)
2014						
Hedged forecast cash flows expected to occur						
Forecast receivable cash flows	155	448	97	—	—	700
Forecast payable cash flows	(26)	(49)	(41)	(67)	(4)	(187)

13 Debt securities

	Group							
	Central and local government				Other financial			Of which
2015	UK £m	US £m	Other £m	Banks £m	institutions £m	Corporate £m	Total £m	ABS (1) £m
Held-for-trading	4,107	4,627	22,222	576	3,591	636	35,759	707
Available-for-sale	9,110	10,265	11,293	1,639	4,670	15	36,992	2,252
Loans and receivables	—	—	—	—	2,221	144	2,365	2,222
Held-to-maturity	4,911	—	—	—	—	—	4,911	—
	18,128	14,892	33,515	2,215	10,482	795	80,027	5,181
Available-for-sale								
Gross unrealised gains	383	104	267	3	105	7	869	88
Gross unrealised losses	(7)	(62)	(9)	(1)	(33)	(3)	(115)	(16)
2014								
Held-for-trading	6,218	7,709	24,448	1,391	7,383	1,979	49,128	3,559
Designated as at fair value through profit or loss	—	—	—	—	1	—	1	—
Available-for-sale	4,747	5,230	9,472	3,276	4,769	46	27,540	3,488
Loans and receivables	—	—	—	179	2,751	138	3,068	2,714
Held-to-maturity	4,537	—	—	—	—	—	4,537	—
	15,502	12,939	33,920	4,846	14,904	2,163	84,274	9,761
Available-for-sale								
Gross unrealised gains	451	144	300	8	142	6	1,051	128
Gross unrealised losses	(1)	(5)	(1)	—	(56)	(2)	(65)	(56)

Note:
(1) Includes asset-backed securities issued by US federal agencies and government sponsored entities, and covered bonds.

Gross gains of £30 million (2014 - £314 million) and gross losses of nil (2014 - £20 million) were realised on the sale of available-for-sale securities in continuing operations.

Gross gains of £11 million (2014 - £20 million) and gross losses of nil (2014 - £3 million) were realised on the sale of available-for-sale securities in discontinued operations.

	Bank							
	Central and local government				Other financial			Of which
2015	UK £m	US £m	Other £m	Banks £m	institutions £m	Corporate £m	Total £m	ABS (1) £m
Held-for-trading	4,107	598	22,221	513	2,768	604	30,811	706
Available-for-sale	9,110	10,265	9,770	1,367	4,708	—	35,220	2,252
Loans and receivables	—	—	—	—	5,516	144	5,660	5,289
Held-to-maturity	4,911	—	—	—	—	—	4,911	—
	18,128	10,863	31,991	1,880	12,992	748	76,602	8,247
Available-for-sale								
Gross unrealised gains	383	104	266	3	101	—	857	88
Gross unrealised losses	(7)	(62)	(9)	(1)	(28)	—	(107)	(16)
2014								
Held-for-trading	6,218	1,283	24,373	1,316	4,447	1,573	39,210	1,390
Available-for-sale	4,627	5,070	7,214	2,523	5,271	20	24,725	3,348
Loans and receivables	—	—	—	179	18,805	138	19,122	18,762
Held-to-maturity	4,537	—	—	—	—	—	4,537	—
	15,382	6,353	31,587	4,018	28,523	1,731	87,594	23,500
Available-for-sale								
Gross unrealised gains	450	144	298	5	141	—	1,038	126
Gross unrealised losses	(1)	(5)	—	—	(56)	—	(62)	(56)

Note:
(1) Includes asset-backed securities issued by US federal agencies and government sponsored entities, and covered bonds.

14 Equity shares

	Group					
	2015			2014		
	Listed £m	Unlisted £m	Total £m	Listed £m	Unlisted £m	Total £m
Held-for-trading	598	3	601	4,699	25	4,724
Designated as at fair value through profit or loss	—	71	71	10	230	240
Available-for-sale	10	387	397	15	224	239
	608	461	1,069	4,724	479	5,203
Available-for-sale						
Gross unrealised gains	5	262	267	5	86	91
Gross unrealised losses	—	(6)	(6)	(4)	(8)	(12)

	Bank					
	2015			2014		
	Listed £m	Unlisted £m	Total £m	Listed £m	Unlisted £m	Total £m
Held-for-trading	597	2	599	4,697	17	4,714
Designated as at fair value through profit or loss	—	—	—	—	40	40
Available-for-sale	6	326	332	4	122	126
	603	328	931	4,701	179	4,880
Available-for-sale						
Gross unrealised gains	3	248	251	2	36	38

Gross gains of £11 million (2014 - £172 million) and gross losses of £1 million (2014 - £63 million) were realised on the sale of available-for-sale equity shares in continuing operations. There were no gains or losses in discontinued operations.

Dividend income from available-for-sale equity shares in continuing operations was £20 million (2014 - £20 million) and in discontinued operations was £15 million (2014 - £22 million).

Unquoted equity investments whose fair value cannot be reliably measured are carried at cost and classified as available-for-sale financial assets.

15 Investments in Group undertakings

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

	Bank	
	2015 £m	2014 £m
At 1 January	39,857	42,328
Currency translation and other adjustments	83	115
Additional investments in Group undertakings	857	2,668
Disposals	(270)	(904)
Impairment of investments	(6,045)	(4,350)
At 31 December	34,482	39,857

The impairment charge for 2015 and 2014 principally relates to the Bank's investment in RBSG International Holdings Limited, the former direct parent of Citizen Financial Group Inc.

The principal subsidiary undertakings of the Bank are shown below. Their capital consists of ordinary and preference shares, which are unlisted with the exception of certain preference shares issued by NatWest. All of the subsidiary undertakings are owned either by the Bank, or directly or indirectly through intermediate holding companies. All of these subsidiaries are included in the Group's consolidated financial statements and have an accounting reference date of 31 December.

	Nature of business	Country of incorporation and principal area of operation
National Westminster Bank Plc (1)	Banking	Great Britain
Coutts & Company (2, 3)	Private Banking	Great Britain
RBS Securities Inc (2)	Broker dealer	US
Ulster Bank Limited (2, 4)	Banking	Northern Ireland

Notes:
(1) The Bank does not hold any of the NatWest preference shares in issue.
(2) Shares are not directly held by the Bank.
(3) Coutts & Company is incorporated with unlimited liability. Its registered office is 440 Strand, London WC2R 0QS.
(4) Ulster Bank Limited and its subsidiary undertakings also operate in the Republic of Ireland.

Full information on all related undertakings is included in Note 41.

16 Intangible assets

2015	Group Goodwill £m	Other (1) £m	Total £m
Cost			
At 1 January	10,061	2,994	13,055
Transfers from fellow subsidiaries	—	5	5
Transfers to disposal groups	(220)	(156)	(376)
Currency translation and other adjustments	(15)	(9)	(24)
Additions	—	613	613
Disposals and write-off of fully amortised assets	—	(1,237)	(1,237)
At 31 December	9,826	2,210	12,036
Accumulated amortisation and impairment			
At 1 January	3,806	1,484	5,290
Transfers to disposal groups	—	(149)	(149)
Currency translation and other adjustments	(27)	(15)	(42)
Disposals and write-off of fully amortised assets	—	(1,149)	(1,149)
Charge for the year			
- continuing operations	—	229	229
Write down of goodwill and other intangible assets			
- continuing operations	498	833	1,331
At 31 December	4,277	1,233	5,510
Net book value at 31 December	5,549	977	6,526

2014	Group Goodwill £m	Other (1) £m	Total £m
Cost			
At 1 January	17,728	4,910	22,638
Transfers from fellow subsidiaries	—	4	4
Transfers to disposal groups	(8,055)	(1,124)	(9,179)
Currency translation and other adjustments	408	36	444
Additions	—	628	628
Disposals and write-off of fully amortised assets	(20)	(1,460)	(1,480)
At 31 December	10,061	2,994	13,055
At 1 January	7,598	2,688	10,286
Transfers from fellow subsidiaries	—	4	4
Transfers to disposal groups	(4,098)	(532)	(4,630)
Currency translation and other adjustments	196	8	204
Disposals and write-off of fully amortised assets	(20)	(1,449)	(1,469)
Charge for the year			
- continuing operations	—	262	262
- discontinued operations	—	100	100
Write down of goodwill and other intangible assets			
- continuing operations	130	393	523
- discontinued operations	—	10	10
At 31 December	3,806	1,484	5,290
Net book value at 31 December	6,255	1,510	7,765

Note:
(1) Principally internally generated software.

	Bank		
2015	Goodwill £m	Internally generated software £m	Total £m
Cost			
At 1 January	100	1,292	1,392
Currency translation and other adjustments	—	(4)	(4)
Transfers from fellow subsidiaries	—	29	29
Additions	—	612	612
Disposals and write-off of fully amortised assets	—	(1,219)	(1,219)
At 31 December	100	710	810
Accumulated amortisation and impairment			
At 1 January	15	460	475
Currency translation and other adjustments	—	(3)	(3)
Transfers from fellow subsidiaries	—	42	42
Disposals and write-off of fully amortised assets	—	(1,131)	(1,131)
Charge for the year	—	158	158
Write down of goodwill and other intangible assets	—	725	725
At 31 December	15	251	266
Net book value at 31 December	85	459	544
2014			
Cost			
At 1 January	113	1,059	1,172
Currency translation and other adjustments	(1)	(19)	(20)
Transfers to subsidiaries	—	(127)	(127)
Additions	—	494	494
Disposals and write-off of fully amortised assets	(12)	(115)	(127)
At 31 December	100	1,292	1,392
Accumulated amortisation and impairment			
At 1 January	28	17	45
Currency translation and other adjustments	(1)	(24)	(25)
Disposals and write-off of fully amortised assets	(12)	(70)	(82)
Charge for the year	—	145	145
Write down of goodwill and other intangible assets	—	392	392
At 31 December	15	460	475
Net book value at 31 December	85	832	917

The Group's goodwill acquired in business combinations is reviewed annually at 30 September for impairment by comparing the recoverable amount of each cash-generating unit (CGU) to which goodwill has been allocated with its carrying value. The Group's goodwill was reviewed at 30 September 2015 and was also subject to a further full review at 31 December 2015 following the changes to the reportable segments described in Note 35.

Impairment testing involves the comparison of the carrying value of a CGU or group of CGUs with its recoverable amount. Recoverable amount is the higher of fair value and value in use. Value in use is the present value of expected future cash flows from the CGU or group of CGUs. Fair value is the price that would be received to sell an asset in an orderly transaction between market participants.

Impairment testing inherently involves a number of judgmental areas: the preparation of cash flow forecasts for periods that are beyond the normal requirements of management reporting; the assessment of the discount rate appropriate to the business; estimation of the fair value of CGUs; and the valuation of the separable assets of each business whose goodwill is being reviewed. Sensitivity to the more significant variables in each assessment are presented in the tables on the following page.

The recoverable amounts for all CGUs at 30 September 2015 and 31 December 2015 were based on value in use, using management's latest five-year forecasts. The long-term growth rates have been based on respective country nominal GDP growth rates. The risk discount rates are based on those observed to be applied to businesses regarded as peers of the CGUs.

The annual review at 30 September 2015 indicated no impairment to goodwill.

Following the changes to the reportable segments, the Group's goodwill was subject to a further full review at 31 December 2015 using revised business forecasts. This resulted in full impairment of the £498 million goodwill relating to Private Banking.

As a result of the changes to the reportable segments in 2015, goodwill of £0.3 billion was allocated to RBS International, £0.2 billion of which was previously reported in Commercial Banking and £0.1 billion of which was previously reported in Private Banking. Goodwill of £0.2 billion was allocated from Private Banking to International Private Banking which had been included within disposal groups since 31 March 2015, see Note 19. In addition, goodwill of £0.1 billion that was written off in 2014 was allocated to Capital Resolution from Corporate & Institutional Banking.

In 2014. the change in reportable segments resulted in the £2.8 billion goodwill attributed to UK Corporate was allocated to Commercial Banking (£2.1 billion), UK Personal & Business Banking (£0.6 billion) and Corporate & Institutional Banking (£0.1 billion). All UK Retail, Wealth and US Retail & Commercial goodwill was allocated to UK Personal & Business Banking, Private Banking and Citizens Financial Group respectively. The goodwill allocated to Corporate & Institutional Banking was written off immediately following re-segmentation

The analysis of goodwill by operating segment is shown in Note 35.

The carrying value of goodwill and amount by which it is exceeded by the recoverable amount is set out below by division along with the key assumptions applied in calculating the recoverable amount and sensitivities to changes in those assumptions.

		Assumptions		Recoverable	Consequential impact of 1% adverse movement in		Consequential impact of 5% adverse movement
31 December 2015	Goodwill £bn	Terminal growth rate %	Pre-tax discount rate %	amount exceeded carrying value £bn	Discount rate £bn	Terminal growth rate £bn	in forecast pre-tax earnings £bn
UK Personal & Business Banking	3.3	4.5	12.0	10.7	(2.6)	(1.5)	(1.7)
Commercial Banking	1.9	4.5	12.1	6.4	(1.9)	(0.9)	(1.2)
RBS International	0.3	4.5	10.2	1.2	(0.5)	(0.3)	(0.2)
30 September 2014							
UK Personal & Business Banking	3.3	4.5	11.5	17.6	(3.6)	(2.5)	(1.6)
Commercial Banking	2.1	4.5	11.7	3.0	(1.9)	(0.9)	(1.0)
Private Banking	0.8	4.5	11.4	0.7	(0.5)	(0.3)	(0.2)
Citizens Financial Group	3.8	5.0	14.4	0.3	(1.1)	(0.7)	(0.7)

Other intangible assets are reviewed for indicators of impairment. In 2015, £833 million (2014 - £401 million) of previously capitalised software was written off by the Group. Previously capitalised software written off by the Bank was £725 million (2014 - £392 million).

17 Property, plant and equipment

2015	Group Investment properties £m	Freehold premises £m	Long leasehold premises £m	Short leasehold premises £m	Computers and other equipment £m	Operating lease assets £m	Total £m
Cost or valuation							
At 1 January	1,933	2,824	213	1,320	2,936	1,551	10,777
Transfers to disposal groups	—	(7)	—	(41)	(25)	—	(73)
Currency translation and other adjustments	(101)	13	(2)	(4)	1	15	(78)
Additions	12	139	8	125	349	202	835
Change in fair value of investment properties							
- continuing operations	13	—	—	—	—	—	13
Disposals and write-off of fully depreciated assets	(951)	(445)	(42)	(152)	(993)	(212)	(2,795)
At 31 December	906	2,524	177	1,248	2,268	1,556	8,679
Accumulated impairment, depreciation and amortisation							
At 1 January	—	986	121	785	2,100	662	4,654
Transfers to disposal groups	—	(3)	—	(24)	(23)	—	(50)
Currency translation and other adjustments	—	7	11	—	(3)	5	20
Write down of property, plant and equipment	—	279	—	—	93	—	372
Disposals and write-off of fully depreciated assets	—	(262)	(38)	(103)	(795)	(144)	(1,342)
Charge for the year							
- continuing operations	—	62	(6)	92	271	153	572
At 31 December	—	1,069	88	750	1,643	676	4,226
Net book value at 31 December	906	1,455	89	498	625	880	4,453
2014							
Cost or valuation							
At 1 January	2,633	2,942	240	1,709	4,192	1,899	13,615
Transfers to disposal groups	—	(131)	—	(275)	(1,034)	(210)	(1,650)
Transfers from fellow subsidiaries	—	—	—	2	6	—	8
Currency translation and other adjustments	(175)	17	(3)	10	52	23	(76)
Reclassifications	—	(8)	—	—	8	—	—
Additions	117	52	2	59	314	230	774
Expenditure on investment properties	13	—	—	—	—	—	13
Change in fair value of investment properties							
- continuing operations	(25)	—	—	—	—	—	(25)
Disposals and write-off of fully depreciated assets	(630)	(48)	(26)	(185)	(602)	(391)	(1,882)
At 31 December	1,933	2,824	213	1,320	2,936	1,551	10,777
Accumulated impairment, depreciation and amortisation							
At 1 January	—	942	137	961	2,939	770	5,749
Transfers to disposal groups	—	(41)	—	(205)	(800)	(55)	(1,101)
Transfers from fellow subsidiaries	—	—	—	1	5	—	6
Currency translation and other adjustments	—	2	(3)	7	42	7	55
Write down of property, plant and equipment	—	4	—	2	4	—	10
Disposals and write-off of fully depreciated assets	—	(20)	(22)	(95)	(437)	(234)	(808)
Charge for the year							
- continuing operations	—	95	9	95	300	165	664
- discontinued operations	—	4	—	19	47	9	79
At 31 December	—	986	121	785	2,100	662	4,654
Net book value at 31 December	1,933	1,838	92	535	836	889	6,123

Investment property valuations principally employ present value techniques that discount expected cash flows. Expected cash flows reflect rental income, occupancy and residual market values; valuations are sensitive to changes in these factors. The fair value measurement of non-specialised properties in locations where the market for such properties is active and transparent are categorised as level 2 - 95% (2014 - 78%); otherwise investment property fair value measurements are categorised as level 3 - 5% (2014 - 22%).

Valuations were carried out by qualified surveyors who are members of the Royal Institution of Chartered Surveyors, or an equivalent overseas body; property with a fair value of £700 million (2014 - £932 million) was valued by independent valuers.

Rental income from investment properties was £79 million (2014 - £217 million). Direct operating expenses of investment properties were £14 million (2014 - £91 million).

	Bank				
2015	Freehold premises £m	Long leasehold premises £m	Short leasehold premises £m	Computers and other equipment £m	Total £m
Cost or valuation					
At 1 January	1,314	76	628	2,483	4,501
Currency translation and other adjustments	(1)	(1)	(1)	(4)	(7)
Additions	49	1	66	228	344
Disposals and write-off of fully depreciated assets	(202)	—	(60)	(972)	(1,234)
At 31 December	1,160	76	633	1,735	3,604
Accumulated impairment, depreciation and amortisation					
At 1 January	409	44	335	1,737	2,525
Currency translation and other adjustments	—	11	—	(3)	8
Write down of property, plant and equipment	—	—	—	81	81
Disposals and write-off of fully depreciated assets	(85)	—	(43)	(803)	(931)
Charge for the year	51	(9)	45	222	309
At 31 December	375	46	337	1,234	1,992
Net book value at 31 December	785	30	296	501	1,612
2014					
Cost or valuation					
At 1 January	1,303	96	723	2,664	4,786
Transfers from fellow subsidiaries	—	—	2	2	4
Currency translation and other adjustments	(1)	(1)	(1)	(4)	(7)
Additions	15	—	29	210	254
Disposals and write-off of fully depreciated assets	(3)	(19)	(125)	(389)	(536)
At 31 December	1,314	76	628	2,483	4,501
Accumulated impairment, depreciation and amortisation					
At 1 January	361	58	335	1,748	2,502
Transfers from fellow subsidiaries	—	—	1	2	3
Currency translation and other adjustments	(1)	—	(2)	(6)	(9)
Disposals and write-off of fully depreciated assets	(1)	(19)	(45)	(272)	(337)
Charge for the year	50	5	46	265	366
At 31 December	409	44	335	1,737	2,525
Net book value at 31 December	905	32	293	746	1,976

18 Prepayments, accrued income and other assets

	Group		Bank	
	2015 £m	2014* £m	2015 £m	2014 £m
Prepayments	392	621	277	516
Accrued income	268	429	107	181
Tax recoverable	150	304	143	52
Pension schemes in net surplus (see Note 4)	215	180	186	159
Interests in associates	306	292	61	62
Other assets	1,688	2,472	775	1,233
	3,019	4,298	1,549	2,203

*Restated - refer to page 148 for further details

19 Discontinued operations and assets and liabilities of disposal groups

In accordance with a commitment to the European Commission to divest Citizens Financial Group, Inc. (Citizens) by 31 December 2016, RBS Group disposed of 30% of its interest in Citizens during the second half of 2014 primarily through an initial public offering in the USA and disposed of further tranches of 28% in March 2015, 21% in August 2015 and the remaining 21% in October 2015 to complete the divestment. Consequently, Citizens is classified as a disposal group and treated as a discontinued operation until October 2015. From 3 August 2015, Citizens was an associated undertaking.

On reclassification to disposal groups at 31 December 2014, the carrying value of Citizens exceeded its fair value less costs to sell (Fair Value Hierarchy level 2: based on the quoted price of shares in Citizens Financial Group, Inc.) by £3,994 million and the carrying value of the assets and liabilities of the disposal group has been adjusted by this amount. This loss was attributed to the intangible assets of the disposal group. The gain on disposal in 2015 comprised £249 million on the derecognition of assets and liabilities, and £1,001 million in respect of reserves reclassified in accordance with IFRS.

(a) Profit/(loss) from discontinued operations, net of tax

	2015 £m	2014 £m	2013 £m
Citizens			
Interest income	1,433	2,204	2,252
Interest expense	(144)	(191)	(288)
Net interest income	1,289	2,013	1,964
Other income	615	1,043	1,056
Total income	1,904	3,056	3,020
Operating expenses	(1,181)	(2,123)	(2,102)
Profit before impairment losses	723	933	918
Impairment losses	(103)	(197)	(312)
Operating profit before tax	620	736	606
Tax charge	(212)	(228)	(196)
Profit after tax	408	508	410
Provision for gain/(loss) on disposal of subsidiary	10	(3,994)	—
Gain on disposal of subsidiary	1,159	—	—
Provision for loss on disposal of interest in associate	(130)	—	—
Gain on disposal of interest in associate	91	—	—
Profit/(loss) from Citizens discontinued operations, net of tax	1,538	(3,486)	410

(b) Cash flows attributable to discontinued operations

Included within the Groups cash flows are the following amounts attributable to discontinued operations.

	2015 £m	2014 £m	2013 £m
Net cash flows from operating activities	(57)	3,997	258
Net cash flows from investing activities	(6)	(4,194)	(1,217)
Net cash flows from financing activities	10	596	(9)
Net (decrease)/increase in cash and cash equivalents	(58)	129	(8)

(c) Assets and liabilities of disposal groups

	Group	
	2015 £m	2014 £m
Assets of disposal groups		
Cash and balances at central banks	535	622
Loans and advances to banks	709	1,745
Loans and advances to customers	1,639	59,606
Debt securities and equity shares	443	15,865
Derivatives	30	402
Intangible assets	—	555
Property, plant and equipment	19	549
Other assets	111	1,689
	3,486	81,033
Liabilities of disposal groups		
Deposits by banks	32	6,794
Customer accounts	2,805	61,256
Debt securities in issue	—	1,625
Derivatives	28	144
Settlement balances	7	—
Subordinated liabilities	—	226
Other liabilities	108	1,239
	2,980	71,284

Disposal groups at 31 December 2015 is primarily International Private Banking (fair value less costs to sell reflects the agreed sale to Union Bancaire Privèe fair value hierarchy level 3) (£3,344 million assets; £2,724 million liabilities).

Disposal groups at 31 December 2014 is predominantly Citizens.

20 Short positions

	Group		Bank	
	2015 £m	2014 £m	2015 £m	2014 £m
Debt securities				
- Government	19,840	20,856	16,769	15,193
- Other issuers	966	1,960	822	1,186
Equity shares	2	212	2	211
	20,808	23,028	17,593	16,590

Note:
(1) All short positions are classified as held-for-trading.

21 Provisions, accruals and other liabilities

	Group		Bank	
	2015 £m	2014 £m	2015 £m	2014 £m
Notes in circulation	1,886	1,803	1,199	1,129
Current tax	186	714	166	540
Accruals	1,876	2,649	1,192	1,666
Deferred income	379	448	226	290
Provisions for liabilities and charges (see tables below)	7,220	4,762	1,847	1,570
Other liabilities	2,523	1,886	1,046	427
	14,070	12,262	5,676	5,622

	Group							
			Regulatory and legal actions					
Provisions for liabilities and charges	Payment Protection Insurance (1) £m	Interest Rate Hedging Products (2) £m	Other customer redress (3) £m	FX investigations (4) £m	Other regulatory provisions (4) £m	Litigation (5) £m	Property and other (6) £m	Total £m
At 1 January 2015	799	424	568	320	183	1,772	696	4,762
Transfer	—	—	—	(15)	(71)	86	—	—
Currency translation and other movements	—	—	—	16	2	105	24	147
Charge to income statement								
- continuing operations	600	81	368	334	27	2,170	1,380	4,960
Releases to income statement								
- continuing operations	(1)	(13)	(34)	—	(7)	(18)	(417)	(490)
Provisions utilised	(402)	(343)	(292)	(349)	(82)	(203)	(488)	(2,159)
At 31 December 2015	996	149	610	306	52	3,912	1,195	7,220

	Bank							
			Regulatory and legal actions					
Provisions for liabilities and charges	Payment Protection Insurance (1) £m	Interest Rate Hedging Products (2) £m	Other customer redress (3) £m	FX investigations (4) £m	Other regulatory provisions (4) £m	Litigation (5) £m	Property and other (6) £m	Total £m
At 1 January 2015	312	154	104	320	97	35	548	1,570
Transfer	—	—	—	(15)	(50)	65	—	—
Currency translation and other movements	—	—	(1)	16	—	1	32	48
Charge to income statement	236	(4)	89	334	—	52	1,106	1,813
Releases to income statement	—	—	(9)	—	(31)	(12)	(435)	(487)
Provisions utilised	(155)	(107)	(47)	(349)	—	(64)	(375)	(1,097)
At 31 December 2015	393	43	136	306	16	77	876	1,847

Notes:

(1) To reflect the developments detailed in Note 29, the Group increased its provision for PPI by £600 million in 2015 (2014 - £650 million), bringing the cumulative charge to £4.3 billion, of which £3.3 billion (77%) in redress had been paid by 31 December 2015. Of the £4.3 billion cumulative charge, £3.9 billion relates to redress and £0.4 billion to administrative expenses.

The principal assumptions underlying the Group's provision in respect of PPI sales are: assessment of the total number of complaints that the Group will receive; the proportion of these that will result in redress; and the average cost of such redress. The number of complaints has been estimated from an analysis of the Group's portfolio of PPI policies sold by vintage and by product. Estimates of the percentage of policyholders that will lodge complaints (the take up rate) and of the number of these that will be upheld (the uphold rate) have been established based on recent experience, guidance in FSA policy statements and the expected rate of responses from proactive customer contact. The average redress assumption is based on recent experience and FSA calculation rules.

The table below shows the sensitivity of the provision to changes in the principal assumptions (all other assumptions remaining the same).

Assumption	Actual to date	Current assumptions	Sensitivity: Change in assumption %	Sensitivity: Consequential change in provision £m
Single premium book past business review take up rate	55%	56%	+/-5	+/-55
Uphold rate (1)	91%	89%	+/-5	+/-35
Average redress	£1,677	£1,638	+/-5	+/-36

Note:
(1) Uphold rates exclude claims where no PPI policy was held.

Interest that will be payable on successful complaints has been included in the provision as has the estimated cost to the Group of administering the redress process. There are uncertainties as to the eventual cost of redress which will depend on actual complaint volumes, take up and uphold rates and average redress costs. Assumptions related to these are inherently uncertain and the ultimate financial impact may be different from the amount provided. We continue to monitor the position closely and refresh the underlying assumptions.

Background information in relation to PPI claims is given in Note 29.

(2) The Group has a provision of £149 million for its liability in respect of the sale of Interest Rate Hedging Products (IRHP), having an incurred cost of £1.5 billion. The provision includes redress that will be paid to customers, consequential loss (including interest) on customer redress, the cost to the Group of exiting the hedging positions and the cost of undertaking the review.

In 2015, the Group increased its provision by £68 million (2014 - £185 million; 2013 - £550 million), principally reflecting a marginal increase in redress experience compared to expectations and the cost of a small number of consequential loss claims over and above interest offered as part of basic redress payments. The outcomes of all cases have now been agreed with the independent skilled person appointed to review all decisions.

The cumulative charge for IRHP is £1.5 billion, of which £1.1 billion relates to redress and £0.4 billion to administrative expenses.

The principal assumptions underlying the Group's provision are:

- the proportion of relevant customers with interest rate caps that will ask to be included in the review;
- the type of consequential loss claims that will be received;
- movements in market rates that will impact the cost of closing out legacy hedging positions; and
- the cost of the review.

Uncertainties remain over the number of transactions that will qualify for redress and the nature and cost of that redress, including the cost of consequential loss claims.

Background information in relation to Interest Rate Hedging Products claims is given in Note 29.

(3) The Group has provided for other customer redress, primarily in relation to investment advice in retail and private banking, £49 million (2014 - £190 million) and packaged accounts, £157 million (2014 - £150 million).

(4) The Group is party to certain legal proceedings and regulatory investigations and continues to co-operate with a number of regulators. All such matters are periodically reassessed with the assistance of external professional advisers, where appropriate, to determine the likelihood of the Group incurring a liability and to evaluate the extent to which a reliable estimate of any liability can be made. An additional charge of £361 million was booked in 2015 (2014 - £820 million; 2013 - £124 million), primarily relating to investigations into the foreign exchange market, regulatory fines in connection with the June 2012 technology incident and other conduct and regulatory matters. Details of these investigations and a discussion of the nature of the associated uncertainties are given in Note 29.

(5) Arising out of its normal business operations, the Group is party to legal proceedings in the United Kingdom, the United States and other jurisdictions. An additional charge of £2.2 billion was recorded in 2015 as a result of greater levels of certainty on expected outcomes, primarily in respect of mortgage-backed securities and securities-related litigation following third party settlements and regulatory decisions. Detailed descriptions of the Group's legal proceedings and discussion of the associated uncertainties are given in Note 29.

(6) The majority of property provisions relate to vacant leasehold property and comprise the present value of the shortfall between rentals payable and rentals receivable from sub-letting. Other provisions include restructuring provisions of £459 million principally termination benefits.

22 Deferred tax

	Group		Bank	
	2015 £m	2014* £m	2015 £m	2014 £m
Deferred tax liability	729	236	—	—
Deferred tax asset	(2,622)	(1,881)	(902)	(733)
Net deferred tax asset	(1,893)	(1,645)	(902)	(733)

Net deferred tax asset comprised:

	Group*											
	Pension £m	Accelerated capital allowances £m	Provisions £m	Deferred gains £m	Fair value of financial instruments £m	Available-for-sale financial assets £m	Intangibles £m	Cash flow hedging £m	Share schemes £m	Tax losses carried forward £m	Other £m	Total £m
At 1 January 2014	(527)	1,261	(1,503)	43	(12)	(15)	225	(1)	(13)	(2,496)	(208)	(3,246)
Transfer to disposal groups	28	(579)	423	—	—	52	(276)	48	—	—	28	(276)
Charge/(credit) to income statement												
- continuing operations	80	(186)	904	(4)	(40)	16	—	(55)	(14)	1,019	113	1,833
- discontinued operations	(6)	33	(38)	—	—	(2)	51	6	—	—	38	82
(Credit)/charge to other comprehensive income	(290)	—	—	—	—	1	—	282	(3)	(12)	—	(22)
Currency translations and other adjustments	—	11	(27)	—	—	(4)	—	—	—	10	(6)	(16)
At 1 January 2015	(715)	540	(241)	39	(52)	48	—	280	(30)	(1,479)	(35)	(1,645)
Acquisitions/(disposals) of subsidiaries	7	(19)	—	(3)	—	(4)	—	—	—	—	(1)	(20)
Charge/(credit) to income statement	160	(289)	(89)	14	48	(44)	—	98	2	135	54	89
(Credit)/charge to other comprehensive income	(314)	—	—	—	—	66	—	(135)	5	—	—	(378)
Currency translations and other adjustments	5	9	3	—	—	23	—	—	—	13	8	61
At 31 December 2015	(857)	241	(327)	50	(4)	89	—	243	(23)	(1,331)	26	(1,893)

	Bank									
	Pension £m	Accelerated capital allowances £m	Provisions £m	Deferred gains £m	Available-for-sale financial assets £m	Cash flow hedging £m	Share schemes £m	Tax losses carried forward £m	Other £m	Total £m
At 1 January 2014	11	(490)	(186)	23	—	100	(25)	(1,693)	(38)	(2,298)
Charge/(credit) to income statement	2	(89)	(9)	(1)	—	7	(1)	1,216	19	1,144
(Credit)/charge to other comprehensive income	(16)	—	—	—	—	101	(3)	(12)	—	70
Acquisitions of businesses	—	350	—	—	—	—	—	—	—	350
Currency translations and other adjustments	—	—	—	—	—	—	—	—	1	1
At 1 January 2015	(3)	(229)	(195)	22	—	208	(29)	(489)	(18)	(733)
Charge/(credit) to income statement	1	(180)	(64)	9	—	13	2	27	18	(174)
Charge/(credit) to other comprehensive income	20	—	—	—	58	(77)	4	—	—	5
At 31 December 2015	18	(409)	(259)	31	58	144	(23)	(462)	—	(902)

*Restated - refer to page 148 for further details

Deferred tax assets in respect of unused tax losses are recognised if the losses can be used to offset probable future taxable profits after taking into account the expected reversal of other temporary differences. Recognised deferred tax assets in respect of tax losses are analysed below.

	2015 £m	2014 £m
UK tax losses carried forward		
- The Royal Bank of Scotland plc	462	489
- National Westminster Bank Plc	628	768
- Ulster Bank Limited	31	—
	1,121	1,257
Overseas tax losses carried forward		
- Ulster Bank Ireland Limited	210	222
	1,331	1,479

UK tax losses

Under UK tax rules, tax losses can be carried forward indefinitely. In periods from April 2015, the Finance Act 2015 limits the offset of losses carried forward by UK banks to 50% of profits. The main rate of UK Corporation Tax will reduce from 20% to 19% from 1 April 2017 and to 18% from 1 April 2020. Under the Finance (No 2) Act 2015, tax losses carried forward at 31 December 2015 are given credit in future periods at the main rate of UK corporation tax, excluding the Banking Surcharge rate (8%) introduced by the Act. Deferred tax assets and liabilities at 31 December 2015 take into account the reduced rates in respect of tax losses and non-banking temporary differences and where appropriate, the banking surcharge inclusive rate in respect of other banking temporary differences.

The Royal Bank of Scotland plc – The Royal Bank of Scotland plc reported a taxable profit in 2011 and tax losses in 2012 and 2013. The tax loss for 2012 reflected the reversal of previous own credit gains offset by core banking profitability. In 2013 UK tax losses were largely attributable to loan impairment charges arising from the accelerated recovery strategy recorded in the final quarter of the period. In 2014, core profitability remained strong and a taxable profit arose. In 2015 a further tax loss arises as a result of restructuring costs incurred as part of RBS's strategic plan. A reduction in the carrying value of deferred tax assets of £701 million was recorded in 2013 with a further reduction of £850 million being recorded in 2014. In addition, deferred tax of £150 million was not recognised in respect of excess 2013 UK taxable losses. Restructuring will continue to constrain the utilisation of carried forward tax losses in the near-term. The Group expects that the balance of recognised deferred tax asset at 31 December 2015 of £462 million in respect of tax losses amounting to £2,433 million will be recovered by the end of 2020.

National Westminster Bank Plc – the deferred tax asset in respect of tax losses at 31 December 2015 relates to residual unrelieved trading losses that arose between 2009 and 2014. 59% of the losses that arose were relieved against taxable profits arising in other UK Group companies. Based on its strategic plan, the Group expects that the recognised deferred tax asset of £628 million in respect of tax losses amounting to £3,307 million will be recovered by the end of 2020.

Overseas tax losses

Ulster Bank Ireland Limited – a deferred tax asset of £210 million has been recognised in respect of losses of £1,678 million (2014 - £1,776 million; 2013 - £592 million) of total tax losses of £7,083 million (2014 - £8,599 million; 2013 - £11,575 million) carried forward at 31 December 2015. These losses arose principally as a result of significant impairment charges between 2008 and 2013 reflecting challenging economic conditions in the Republic of Ireland. Impairment charges have reduced and Ulster Bank Ireland Limited returned to profitability during 2014 and 2015. Based on RBS Group's strategic plan, the losses on which a deferred tax asset has been recognised will be utilised against future taxable profits by the end of 2022.

Unrecognised deferred tax

Deferred tax assets of £4,364 million (2014 - £3,778 million; 2013 - £2,723 million) have not been recognised in respect of tax losses and other temporary differences carried forward of £19,499 million (2014 - £18,760 million; 2013 - £19,145 million) in jurisdictions where doubt exists over the availability of future taxable profits. Of these losses and other temporary differences, £55 million expire within five years and £4,920 million thereafter . The balance of tax losses and other temporary differences carried forward has no expiry date.

Deferred tax liabilities of £256 million (2014 - £186 million; 2013 - £186 million) have not been recognised in respect of retained earnings of overseas subsidiaries and held-over gains on the incorporation of overseas branches. Retained earnings of overseas subsidiaries are expected to be reinvested indefinitely or remitted to the UK free from further taxation. No taxation is expected to arise in the foreseeable future in respect of held-over gains. Changes to UK tax legislation largely exempts from UK tax, overseas dividends received on or after 1 July 2009.

23 Subordinated liabilities

Certain preference shares issues are classified as liabilities; these securities remain subject to the capital maintenance rules of the Companies Act 2006.

The following tables analyse the remaining contracted maturity of subordinated liabilities by the final redemption date and by the next call date.

	Group		Bank	
	2015 £m	2014 £m	2015 £m	2014 £m
Dated loan capital	15,870	19,459	15,470	17,639
Undated loan capital	8,179	8,170	7,401	7,312
Preference shares	2,981	2,840	2,663	2,529
	27,030	30,469	25,534	27,480

	Group						
2015 - final redemption	2016 £m	2017 £m	2018-2020 £m	2021-2025 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	34	—	4,999	369	—	4,661	10,063
US dollar	91	—	339	4,632	1,062	4,952	11,076
Euro	167	648	1,621	2,245	—	184	4,865
Other	30	—	18	737	—	241	1,026
	322	648	6,977	7,983	1,062	10,038	27,030

	Group							
2015 - call date	Currently £m	2016 £m	2017 £m	2018-2020 £m	2021-2025 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	2,560	5,073	51	1,655	483	45	196	10,063
US dollar	2,011	1,055	2,919	339	3,289	1,463	—	11,076
Euro	—	1,063	1,063	2,372	320	—	47	4,865
Other	26	263	737	—	—	—	—	1,026
	4,597	7,454	4,770	4,366	4,092	1,508	243	27,030

	Group						
2014 - final redemption	2015 £m	2016 £m	2017-2019 £m	2020-2021 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	715	—	4,999	381	—	4,668	10,763
US dollar	530	—	400	5,326	1,222	4,703	12,181
Euro	791	—	2,502	2,416	—	195	5,904
Other	525	—	19	796	—	281	1,621
	2,561	—	7,920	8,919	1,222	9,847	30,469

	Group							
2014 - call date	Currently £m	2015 £m	2016 £m	2017-2019 £m	2020-2024 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	2,559	5,699	57	1,712	495	45	196	10,763
US dollar	1,841	1,766	—	3,019	4,049	1,506	—	12,181
Euro	—	955	834	3,728	338	—	49	5,904
Other	8	526	273	814	—	—	—	1,621
	4,408	8,946	1,164	9,273	4,882	1,551	245	30,469

23 Subordinated liabilities continued

	Bank						
2015 - final redemption	2016 £m	2017 £m	2018-2020 £m	2021-2025 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	24	—	4,999	—	—	4,406	9,429
US dollar	87	—	339	4,632	1,062	4,305	10,425
Euro	166	648	1,621	2,245	—	—	4,680
Other	30	—	—	737	—	233	1,000
	307	648	6,959	7,614	1,062	8,944	25,534

	Bank							
2015 - call date	Currently £m	2016 £m	2017 £m	2018-2020 £m	2021-2025 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	2,560	5,063	51	1,655	25	45	30	9,429
US dollar	1,838	577	2,919	339	3,289	1,463	—	10,425
Euro	—	925	1,063	2,372	320	—	—	4,680
Other	—	263	737	—	—	—	—	1,000
	4,398	6,828	4,770	4,366	3,634	1,508	30	25,534

	Bank						
2014 - final redemption	2015 £m	2016 £m	2017-2019 £m	2020-2024 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	292	—	4,999	-	—	4,415	9,706
US dollar	526	—	400	4,454	1,008	4,084	10,472
Euro	790	—	2,502	2,416	—	—	5,708
Other	525	—	-	796	—	273	1,594
	2,133	—	7,901	7,666	1,008	8,772	27,480

	Bank							
2014 - call date	Currently £m	2015 £m	2016 £m	2017-2019 £m	2020-2024 £m	Thereafter £m	Perpetual £m	Total £m
Sterling	2559	5,277	57	1,712	26	45	30	9,706
US dollar	1,841	1,143	—	3,019	3,177	1,292	—	10,472
Euro	—	808	834	3,728	338	—	—	5,708
Other	—	525	273	796	—	—	—	1,594
	4,400	7,753	1,164	9,255	3,541	1,337	30	27,480

23 Subordinated liabilities continued

Issuances and redemptions during the year (value at date of transaction) are set out below.

	Capital treatment	2015 £m	2014 £m
New issues			
The Royal Bank of Scotland plc			
€1,000 million 3.63% dated notes 2024	Tier 2	—	833
Charter One Financial, Inc			
US$333 million 4.15% dated notes 2024 (1)	Tier 2	—	195
US$333 million 4.02% dated notes 2024 (1)	Tier 2	—	201
US$334 million 4.08% dated notes 2025 (1)	Tier 2	—	209
		—	1,438
Redemptions			
The Royal Bank of Scotland plc			
€23 million floating rate dated notes	Ineligible	17	—
US$675 million 5.05% dated notes	Ineligible	445	—
AUD18 million floating rate dated notes	Ineligible	9	—
AUD36 million floating rate dated notes	Ineligible	18	—
US$238 million floating rate dated notes	Ineligible	154	—
€750 million 4.88% dated notes	Tier 2	546	—
£250 million 9.63% dated notes	Tier 2	250	—
CHF400 million 2.38% dated notes	Tier 2	259	—
CHF100 million 2.38% dated notes	Tier 2	65	—
CHF200 million 2.38% dated notes	Tier 2	129	—
US$750 million 5.00% dated notes	Tier 2	—	463
US$250 million 5.00% dated notes	Tier 2	—	154
AUD397 million floating rate dated notes	Tier 2	—	217
AUD265 million floating rate dated notes	Tier 2	—	145
CAD217 million floating rate dated notes	Tier 2	—	94
US$322 million floating rate dated notes	Tier 2	—	177
US$229 million floating rate dated notes	Tier 2	—	144
US$686 million floating rate dated notes	Tier 2	—	431
€227 million floating rate notes	Tier 2	—	179
CHF34 million floating rate dated notes	Tier 2	—	23
£56 million 6.00% undated notes	Tier 2	—	56
€176 million floating rate undated notes	Tier 2	—	138
€170 million floating rate undated notes	Tier 2	—	133
£1 million floating rate undated notes	Tier 2	—	1
AUD32 million floating rate notes 2017 (partial redemption)	Tier 2	—	17
AUD53.7 million floating rate notes 2017 (partial redemption)	Tier 2	—	29
€79.75 million floating rate notes 2017 (partial redemption)	Tier 2	—	65
US$211.9 million floating rate notes 2017 (partial redemption)	Tier 2	—	129
€1,250 million perpetual regulated securities	Tier 1	—	1,002
US$850 million non-cumulative preference shares of US$0.01, Series M	Tier 1	—	524
National Westminster Bank Plc			
£87 million 7.63% undated notes	Tier 2	87	—
£300 million 7.88% dated notes	Tier 2	300	—
Ulster Bank Ireland Ltd			
£60 million floating rate notes 2018	Tier 2	—	60
		2,279	4,181

Note:
(1) Transferred to disposal groups at 31 December 2014.

23 Subordinated liabilities continued

Dated loan capital	Capital treatment	2015 £m	2014 £m
The Royal Bank of Scotland plc			
£250 million 9.63% notes 2015 (redeemed June 2015)	Tier 2	—	268
€750 million 4.88% notes 2015 (redeemed April 2015)	Tier 2	—	611
CHF400 million 2.38% notes 2015 (redeemed November 2015)	Tier 2	—	270
CHF100 million 2.38% notes 2015 (redeemed November 2015)	Tier 2	—	65
CHF200 million 2.38% notes 2015 (redeemed November 2015)	Tier 2	—	130
€100 million floating rate notes 2017	Tier 2	73	78
€23 million floating rate notes 2017 (redeemed January 2015)	Ineligible	—	18
€750 million 4.35% notes 2017	Tier 2	597	654
AUD18 million floating rate notes 2017 (redeemed February 2015)	Ineligible	—	9
AUD36 million floating rate notes 2017 (redeemed February 2015)	Ineligible	—	19
US$238 million floating rate notes 2017 (redeemed February 2015)	Ineligible	—	153
€2,000 million 6.93% notes 2018	Tier 2	1,695	1,855
US$125.6 million floating rate notes 2020	Tier 2	85	81
€1,000 million 4.63% notes 2021 (callable quarterly)	Ineligible	767	844
€300 million floating rate notes 2022	Tier 2	207	215
€144.4 million floating rate notes 2023	Tier 2	120	130
AUD883 million 13.13% notes 2022 (callable once March 2017)	Tier 2	461	497
CAD420 million 10.50% notes 2022 (callable once March 2017)	Tier 2	212	241
CHF124 million 9.38% notes 2022 (callable once March 2017)	Tier 2	92	88
€564 million 10.50% notes 2022 (callable once March 2017)	Tier 2	450	478
US$2,132 million 9.50% notes 2022 (callable once March 2017)	Tier 2	1,475	1,401
Due to the holding company			
US$675 million 5.05% notes 2015 (redeemed January 2015) (1)	Tier 2	—	443
US$350 million 4.70% notes 2018 (1)	Tier 2	260	252
£5,000 million floating notes 2019 (callable quarterly) (1)	Tier 2	5,000	5,000
US$2,250 million 6.22% notes 2022 (1)	Tier 2	1,490	1,393
US$389 million 6.10% notes 2023 (1)	Tier 2	276	260
US$2,000 million 6.00% notes 2023 (1)	Tier 2	1,439	1,362
€1,000 million 3.63% notes 2024 (callable once March 2019) (1)	Tier 2	771	824
		15,470	17,639

Notes:
(1) On-lent from The Royal Bank of Scotland Group plc on a subordinated basis.
(2) In the event of certain changes in tax laws, dated loan capital issues may be redeemed in whole, but not in part, at the option of the issuer, at the principal amount thereof plus accrued interest, subject to prior regulatory approval.
(3) Except as stated above, claims in respect of the Group's dated loan capital are subordinated to the claims of other creditors. None of the Group's dated loan capital is secured.
(4) Interest on all floating rate subordinated notes is calculated by reference to market rates.

23 Subordinated liabilities continued

Undated loan capital	Capital treatment	2015 £m	2014 £m
The Royal Bank of Scotland plc			
£31 million 4.96% notes	Ineligible	31	31
£51 million 6.25% notes (callable every five years from December 2017)	Ineligible	51	51
£54 million 5.13% notes (callable every five years from March 2016)	Ineligible	57	59
£35 million 5.50% notes (callable every five years from December 2019)	Ineligible	38	39
£21 million 6.20% notes (callable every five years from March 2022)	Ineligible	26	27
£103 million 9.50% notes (callable every five years from August 2018) (1)	Ineligible	121	126
£16 million 5.63% notes (callable every five years from September 2026) (1)	Ineligible	24	25
£19 million 5.63% notes (callable every five years from June 2032)	Ineligible	21	21
CAD474 million 5.37% fixed rate notes (callable May 2016)	Ineligible	235	275
Due to the holding company			
US$350 million floating rate primary capital notes (callable annually) (2)	Tier 2	236	224
US$1200 million 7.65% perpetual regulatory securities (callable September 2031) (2,3)	Tier 1	821	779
£1,500 million floating rate perpetual notes (callable June 2018) (2)	Tier 2	1,500	1,500
$600 million floating rate perpetual notes (callable June 2018) (2)	Tier 2	405	384
$1,600 million floating rate perpetual notes (callable June 2018) (2)	Tier 2	1,079	1,025
£940 million floating rate perpetual notes (callable) (2)	Tier 2	950	949
US$150 million 8.00% perpetual notes (callable from October 2093) (2)	Tier 2	103	98
US$136 million 7.75% perpetual notes (callable from May 2023) (2)	Tier 2	93	89
£200 million floating rate perpetual notes (callable) (2)	Tier 2	200	200
£885 million floating rate perpetual notes (callable) (2)	Tier 2	886	886
£100 million floating rate perpetual notes (callable) (2)	Tier 2	100	100
£420 million floating rate perpetual notes (callable) (2)	Tier 2	424	424
		7,401	7,312

Notes:
(1) Guaranteed by the company.
(2) On-lent from The Royal Bank of Scotland Group plc on a subordinated basis.
(3) The company can satisfy interest payment obligations by issuing sufficient ordinary shares to appointed Trustees to enable them, on selling these shares, to settle the interest payment.
(4) Except as stated above, claims in respect of the Group's undated loan capital are subordinated to the claims of other creditors. None of the Group's undated loan capital is secured.
(5) In the event of certain changes in tax laws, undated loan capital issues may be redeemed in whole, but not in part, at the option of the Group, at the principal amount thereof plus accrued interest, subject to prior regulatory approval.
(6) Interest on all floating rate subordinated notes is calculated by reference to market rates.

Preference shares (1)	Capital treatment	2015 £m	2014 £m
The Royal Bank of Scotland plc			
Non-cumulative preference shares of US$0.01			
US$200 million 7.65% Series F (callable anytime)	Ineligible	135	128
US$300 million 7.25% Series H (callable anytime)	Ineligible	202	192
US$750 million 6.80% Series L (callable anytime)	Ineligible	506	480
US$650 million 6.43% Series N (callable January 2034)	Ineligible	556	528
US$850 million 5.75% Series R (callable quarterly)	Ineligible	573	544
US$1,000 million 9.12% Series 1 (callable anytime)	Ineligible	691	657
		2,663	2,529

Note:
(1) Issued to the holding company on terms which, in general, mirror the original issues by the holding company.

24 Share capital and reserves

	Allotted, called up and fully paid	
	2015	2014
	£m	£m
Ordinary shares of £1	6,609	6,609

	Allotted, called up and fully paid	
Number of shares - millions	2015	2014
Ordinary shares of £1	6,609	6,609
Non-cumulative preference shares of US$0.01	59	59
Non-cumulative preference shares of €0.01	1	1

Ordinary shares

In 2013, one ordinary share was issued at a premium of £209 million on the cross-border merger with RBS Bank (Romania) S.A. in connection with the transfer of RBS N.V.'s Romania businesses to the company.

No other ordinary shares were issued during 2015 or 2014.

The Bank did not pay an ordinary dividend in 2015 or 2014.

Preference shares

In 2014, the 850,000 Series M non-cumulative preference shares of US$0.01 issued to the holding company were redeemed.

Reserves

At 31 December 2015, the merger reserve comprises of the premium paid to acquire the assets and liabilities of RBS N.V.'s Korean business and the premium on shares issued to acquire NatWest less goodwill amortisation charged under previous GAAP. No share premium was recorded in the Bank financial statements through the operation of the merger relief provisions of the Companies Act 1985.

UK law prescribes that only reserves of the Bank are taken into account for the purpose of making distributions and the permissible applications of the share premium account.

The Group optimises capital efficiency by maintaining reserves in subsidiaries, including regulated entities. Certain preference shares and subordinated debt are also included within regulatory capital. The remittance of reserves to the parent or the redemption of shares or subordinated capital by regulated entities may be subject to maintaining the capital resources required by the relevant regulator.

25 Leases

Year in which receipt will occur	Finance lease contracts and hire purchase agreements: Gross amounts £m	Present value adjustments £m	Other movements £m	Present value £m	Operating lease assets: future minimum lease rentals £m
2015					
Within 1 year	3,111	(236)	(31)	2,844	166
After 1 year but within 5 years	4,801	(420)	(83)	4,298	294
After 5 years	2,784	(1,120)	(24)	1,640	72
Total	10,696	(1,776)	(138)	8,782	532
2014					
Within 1 year	3,028	(227)	(20)	2,781	175
After 1 year but within 5 years	4,916	(445)	(85)	4,386	297
After 5 years	2,998	(1,239)	(37)	1,722	86
Total	10,942	(1,911)	(142)	8,889	558

	Group 2015 £m	2014 £m
Nature of operating lease assets on the balance sheet		
Transportation	556	570
Cars and light commercial vehicles	56	49
Other	268	270
	880	889
Amounts recognised as income and expense		
Finance leases - contingent rental income	(81)	(85)
Operating leases - minimum rentals payable	239	249
Finance lease contracts and hire purchase agreements		
Accumulated allowance for uncollectable minimum receivables	65	104

Amounts recognised as income and expense in discontinued operations was £75 million (2014 - £124 million; 2013 - £134 million) in relation to operating leases – minimum rentals payable.

Residual value exposures

The table below gives details of the unguaranteed residual values included in the carrying value of finance leases receivables (refer to page 176) and operating lease assets (refer to page 211).

	Year in which residual value will be recovered				
2015	Within 1 year £m	After 1 year but within 2 years £m	After 2 years but within 5 years £m	After 5 years £m	Total £m
Operating leases					
- transportation	126	57	52	108	343
- cars and light commercial vehicles	8	3	10	—	21
- other	24	29	35	2	90
Finance lease contracts	30	22	58	24	134
Hire purchase agreements	1	—	3	—	4
	189	111	158	134	592
2014					
Operating leases					
- transportation	24	122	92	99	337
- cars and light commercial vehicles	10	4	6	—	20
- other	24	26	38	6	94
Finance lease contracts	20	24	59	37	140
Hire purchase agreements	—	1	2	—	3
	78	177	197	142	594

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

26 Structured entities

A structured entity (SE) is an entity that has been designed such that voting or similar rights are not the dominant factor in deciding who controls the entity, for example, when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. SEs are usually established for a specific, limited purpose, they do not carry out a business or trade and typically have no employees. They take a variety of legal forms - trusts, partnerships and companies - and fulfil many different functions. As well as being a key element of securitisations, SEs are also used in fund management activities to segregate custodial duties from the fund management advice.

Consolidated structured entities

Securitisations

In a securitisation, assets, or interests in a pool of assets, are transferred generally to a SE which then issues liabilities to third party investors. The majority of securitisations are supported through liquidity facilities or other credit enhancements. The Group arranges securitisations to facilitate client transactions and undertakes own asset securitisations to sell or to fund portfolios of financial assets. The Group also acts as an underwriter and depositor in securitisation transactions in both client and proprietary transactions.

The Group's involvement in client securitisations takes a number of forms. It may: sponsor or administer a securitisation programme; provide liquidity facilities or programme-wide credit enhancement; and purchase securities issued by the vehicle.

Own asset securitisations

In own-asset securitisations, the pool of assets held by the SE is either originated by the Group, or (in the case of whole loan programmes) purchased from third parties.

The table below analyses the asset categories for those own-asset securitisations where the transferred assets continue to be recorded on the Group's balance sheet.

	Group							
	2015				2014			
		Debt securities in issue				Debt securities in issue		
Asset type	Assets £m	Held by third parties £m	Held by the Group (1) £m	Total £m	Assets £m	Held by third parties £m	Held by the Group (1) £m	Total £m
Mortgages								
- UK	3,954	961	3,067	4,028	11,992	3,543	9,877	13,420
- Irish	7,395	1,472	6,836	8,308	8,593	1,697	7,846	9,543
UK credit cards	—	—	—	—	2,717	—	1,567	1,567
Other loans (2)	46	9	—	9	4,995	4	5,245	5,249
	11,395	2,442	9,903	12,345	28,297	5,244	24,535	29,779
Cash deposits	1,201				4,616			
	12,596				32,913			

Notes:
(1) Debt securities retained by the Group may be pledged with central banks.
(2) Corporate, social housing and student loans.

Commercial paper conduits

The Group consolidates a number of asset-backed commercial paper (ABCP) conduits. A conduit is an SE that issues commercial paper and uses the proceeds to purchase or fund a pool of assets. The commercial paper is secured on the assets and is redeemed by further commercial paper issuance, repayment of assets or funding from liquidity facilities. Commercial paper is typically short-dated, usually up to three months. At 31 December 2015, assets held by the conduits totalled £0.6 billion (2014 - £0.6 billion). At 31 December 2015 and 31 December 2014 the conduits were funded entirely by the Group.

Covered bond programme

Certain loans and advances to customers have been assigned to bankruptcy remote limited liability partnership to provide security for issues of debt securities by the Group. The Group retains all of the risks and rewards of these loans, the partnerships are consolidated, the loans retained on the Group's balance sheet and the related covered bonds included within debt securities in issue. At 31 December 2015, £11,207 million of mortgages provided security for debt securities in issue of £5,585 million (2014: mortgages - £13,401 million, bonds - £7,114 million).

26 Structured entities continued

Unconsolidated structured entities

The Group's interests in unconsolidated structured entities are analysed below.

2015	Asset backed securitisation vehicles £m	Investment funds and other £m	Total £m
Held for trading			
Loans and advances to customers	131	—	131
Debt securities	455	73	528
Equity shares	—	111	111
Derivatives assets	548	13	561
Derivatives liabilities	(150)	(23)	(173)
Total	984	174	1,158
Other than held-for-trading			
Loans and advances to customers	2,663	2	2,665
Debt securities	3,153	123	3,276
Total	5,816	125	5,941
Liquidity facilities/loan commitments	1,362	—	1,362
Maximum exposure	8,162	299	8,461

2014	£m	£m	£m
Held for trading			
Loans and advances to customers	449	22	471
Debt securities	3,849	3	3,852
Equity shares	—	310	310
Derivatives assets	1,670	10	1,680
Derivatives liabilities	(850)	(28)	(878)
Total	5,118	317	5,435
Other than held-for-trading			
Loans and advances to customers	5,550	—	5,550
Debt securities	5,524	131	5,655
Total	11,074	131	11,205
Liquidity facilities/loan commitments	2,760	—	2,760
Guarantees	71	—	71
Maximum exposure	19,023	448	19,471

Notes:

(1) Net income arising from interests in unconsolidated structured entities includes interest receivable, trading income as a result of changes in fair value, foreign exchange gains/losses and other income less impairments.

(2) A sponsored entity is a structured entity, established by the Group where the Group provides liquidity and/or credit enhancements or provides ongoing services to the entity. The Group can act as sponsor for its own or for customers' transactions.

(3) In 2015, no assets were transferred into sponsored structured entities (2014 - £1,756 million) which are not consolidated by the Group and to which the Group held no interest at 31 December 2015. Income arising from sponsored entities where no interest was held at year end was losses of £68 million (2014 - gains £172 million).

27 Asset transfers

Under IAS 39 a financial asset is transferred if the Group either (a) transfers the contractual rights to receive the asset's cash flows; or (b) retains the right to the asset's cash flows but assumes a contractual obligation to pay those cash flows to a third party. Following a transfer the financial asset will be derecognised; not derecognised and retained in full on the Group's balance sheet; or continue to be recognised on the balance sheet to the extent of the Group's continuing involvement.

Transfers that do not qualify for derecognition

Securities repurchase agreements and lending transactions

The Group enters into securities repurchase agreements and securities lending transactions under which it transfers securities in accordance with normal market practice.

Generally, the agreements require additional collateral to be provided if the value of the securities falls below a predetermined level. Under standard terms for repurchase transactions in the UK and US markets, the recipient of collateral has an unrestricted right to sell or repledge it, subject to returning equivalent securities on settlement of the transaction.

Securities sold under repurchase transactions are not derecognised if the Group retains substantially all the risks and rewards of ownership. The fair value (and carrying value) of securities transferred under such repurchase transactions included on the balance sheet, are set out below. All of these securities could be sold or repledged by the holder.

	Group		Bank	
Assets subject to securities repurchase agreements or security lending transactions	2015 £m	2014 £m	2015 £m	2014 £m
Debt securities	20,224	22,923	16,484	14,332
Equity shares	9	2,557	2	2,557

The following table provides analyses of assets that have been transferred but have failed the derecognition rules under IAS 39 and therefore continue to be recognised on the Bank's balance sheet.

	Bank	
Asset type	2015 £m	2014 £m
UK mortgages	2,722	8,996
UK credit cards	—	938
Other loans (2)	—	3,122
	2,722	13,056

Notes:
(1) The fair value of the transferred assets is £2,725 million (2014 - £12,823 million) where recourse is to these assets only.
(2) Comprises corporate, social housing and student loans.

Assets pledged as collateral

The Group pledges collateral with its counterparties in respect of derivative liabilities and bank and other borrowings.

	Group		Bank	
Assets pledged against liabilities	2015 £m	2014 £m	2015 £m	2014 £m
Loans and advances to banks	11,477	11,723	10,843	10,845
Loans and advances to customers	17,595	22,166	17,170	21,766
Securities	14,414	9,493	14,414	9,351
	43,486	43,382	42,427	41,962
Liabilities secured by assets				
Deposits by banks	293	461	—	—
Customer accounts	—	130	—	—
Derivatives	31,093	38,876	30,865	38,463
	31,386	39,467	30,865	38,463

28 Capital resources

Under Capital Requirements Regulation (CRR), regulators within the European Union monitor capital on a legal entity basis, with local transitional arrangements on the phasing in of end-point CRR. The capital resources based on the relevant transitional basis for the significant legal entities within the Group are set out below.

	2015			2014		
	RBS plc £m	NatWest Plc £m	UBIL £m	RBS plc £m	NatWest Plc £m	UBIL £m
Shareholders' equity						
Shareholders' equity	51,177	11,282	5,753	52,553	13,312	5,081
Preference shares - equity	(1,421)	—	—	(1,421)	—	—
	49,756	11,282	5,753	51,132	13,312	5,081
Regulatory adjustments and deductions						
Own credit	17	—	—	659	—	—
Defined benefit pension fund adjustment	(138)	—	142	(127)	—	320
Cash flow hedging reserve	(286)	1	—	(755)	3	—
Deferred tax assets	(252)	(622)	(210)	(258)	(742)	—
Prudential valuation adjustments	(349)	(1)	—	(324)	(1)	—
Goodwill and other intangible assets	(544)	(498)	—	(917)	(530)	—
Expected losses less impairments	(395)	(703)	(22)	(805)	(785)	(3)
Instruments of financial sector entities where the institution has a significant investment	(15,680)	(2,413)	—	(14,809)	(2,318)	—
Significant investments in excess of secondary capital	—	(424)	—	—	—	—
Other regulatory adjustments	287	532	27	703	529	(1,217)
	(17,340)	(4,128)	(63)	(16,633)	(3,844)	(900)
CET1 capital	32,416	7,154	5,690	34,499	9,468	4,181
Additional Tier 1 capital						
Qualifying instruments and related share premium subject to phase out	3,493	204	—	3,503	234	—
Tier 1 deductions						
Instruments of financial sector entities where the institution has a significant investment	(1,175)	(187)	—	(1,291)	(140)	—
Tier 1 capital	34,734	7,171	5,690	36,711	9,562	4,181
Qualifying Tier 2 capital						
Qualifying instruments and related share premium	19,039	5,058	492	20,427	5,380	528
Tier 2 deductions						
Instruments of financial sector entities where the institution has a significant investment	(2,432)	(92)	—	(1,836)	(102)	—
Other regulatory adjustments	—	—	(7)	(41)	(8)	(5)
	(2,432)	(92)	(7)	(1,877)	(110)	(5)
Tier 2 capital	16,607	4,966	485	18,550	5,270	523
Total regulatory capital	51,341	12,137	6,175	55,261	14,832	4,704

Note:
(1) Regulatory capital for 2014 has not been impacted by the change in accounting policy for pensions.

In the management of capital resources, the Group is governed by the RBS Group's policy to maintain a strong capital base, to expand it as appropriate and to utilise it efficiently throughout its activities to optimise the return to shareholders while maintaining a prudent relationship between the capital base and the underlying risks of the business. In carrying out this policy, the RBS Group has regard to the supervisory requirements of the PRA. The PRA uses risk asset ratio (RAR) as a measure of capital adequacy in the UK banking sector, comparing a bank's capital resources with its risk-weighted assets (the assets and off-balance sheet exposures are 'weighted' to reflect the inherent credit and other risks); by international agreement, the RAR should be not less than 8% with a Tier 1 component of not less than 4%. The Group has complied with the PRA's capital requirements throughout the year.

A number of subsidiaries and sub-groups within the Group, principally banking entities, are subject to various individual regulatory capital requirements in the UK and overseas. Furthermore, the payment of dividends by subsidiaries and the ability of members of the RBS Group to lend money to other members of the RBS Group may be subject to restrictions such as local regulatory or legal requirements, the availability of reserves and financial and operating performance.

29 Memorandum items

Contingent liabilities and commitments

The amounts shown in the table below are intended only to provide an indication of the volume of business outstanding at 31 December 2015. Although the Group is exposed to credit risk in the event of non-performance of the obligations undertaken by customers, the amounts shown do not, and are not intended to, provide any indication of the Group's expectation of future losses.

	Group		Bank	
	2015 £m	2014 £m	2015 £m	2014 £m
Contingent liabilities and commitments				
Guarantees and assets pledged as collateral security	5,894	11,694	4,534	8,399
Other contingent liabilities	6,789	9,221	5,363	7,755
Standby facilities, credit lines and other commitments	137,364	213,952	88,640	128,193
	150,047	234,867	98,537	144,347

Note:
(1) In the normal course of business, the Bank guarantees specified third party liabilities of certain subsidiaries; it also gives undertakings that individual subsidiaries will fulfil their obligations to third parties under contractual or other arrangements.

Banking commitments and contingent obligations, which have been entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities. The Group's maximum exposure to credit loss, in the event of its obligation crystallising and all counterclaims, collateral or security proving valueless, is represented by the contractual nominal amount of these instruments included in the table above. These commitments and contingent obligations are subject to the Group's normal credit approval processes.

Guarantees - the Group gives guarantees on behalf of customers. A financial guarantee represents an irrevocable undertaking that the Group will meet a customer's specified obligations to a third party if the customer fails to do so. The maximum amount that the Group could be required to pay under a guarantee is its principal amount as in the table above. The Group expects most guarantees it provides to expire unused.

Other contingent liabilities - these include standby letters of credit, supporting customer debt issues and contingent liabilities relating to customer trading activities such as those arising from performance and customs bonds, warranties and indemnities.

Standby facilities and credit lines - under a loan commitment the Group agrees to make funds available to a customer in the future. Loan commitments, which are usually for a specified term may be unconditionally cancellable or may persist, provided all conditions in the loan facility are satisfied or waived. Commitments to lend include commercial standby facilities and credit lines, liquidity facilities to commercial paper conduits and unutilised overdraft facilities.

Other commitments - these include documentary credits, which are commercial letters of credit providing for payment by the Group to a named beneficiary against presentation of specified documents, forward asset purchases, forward deposits placed and undrawn note issuance and revolving underwriting facilities, and other short-term trade related transactions.

Capital Support Deed

The Bank, together with other members of the RBS Group, is party to a Capital Support Deed (CSD). Under the terms of the CSD, the Bank may be required, if compatible with its legal obligations, to make distributions on, or repurchase or redeem, its ordinary shares. The amount of this obligation is limited to the Bank's capital resources in excess of the capital and financial resources needed to meet its regulatory requirements. The Bank may also be obliged to make onward distribution to its ordinary shareholders of dividends or other capital distributions received from subsidiaries that are party to the CSD. The CSD also provides that, in certain circumstances, funding received by the Bank from other parties to the CSD becomes immediately repayable, such repayment being limited to the Bank's available resources.

29 Memorandum items

Contractual obligations for future expenditure not provided for in the accounts

The following table shows contractual obligations for future expenditure not provided for in the accounts at the year end.

	Group		Bank	
	2015 £m	2014 £m	2015 £m	2014 £m
Operating leases				
Minimum rentals payable under non-cancellable leases (1)				
- within 1 year	232	237	141	145
- after 1 year but within 5 years	759	784	501	504
- after 5 years	2,006	2,110	1,407	1,492
	2,997	3,131	2,049	2,141
Capital expenditure on property, plant and equipment	59	35	29	34
Contracts to purchase goods or services (2)	1,442	1,827	1,414	1,789
	4,498	4,993	3,492	3,964

Notes:
(1) Predominantly property leases.
(2) Of which due within 1 year: Group - £302 million (2014 - £389 million) and Bank - £282 million (2014 - £364 million).

Trustee and other fiduciary activities

In its capacity as trustee or other fiduciary role, the Group may hold or place assets on behalf of individuals, trusts, companies, pension schemes and others. The assets and their income are not included in the Group's financial statements. The Group earned fee income of £272 million (2014 - £373 million; 2013 - £408 million) from these activities.

The Financial Services Compensation Scheme

The Financial Services Compensation Scheme (FSCS), the UK's statutory fund of last resort for customers of authorised financial services firms, pays compensation if a firm is unable to meet its obligations. The FSCS funds compensation for customers by raising management expenses levies and compensation levies on the industry. In relation to protected deposits, each deposit-taking institution contributes towards these levies in proportion to their share of total protected deposits on 31 December of the year preceding the scheme year (which runs from 1 April to 31 March), subject to annual maxima set by the Prudential Regulation Authority. In addition, the FSCS has the power to raise levies on a firm that has ceased to participate in the scheme and is in the process of ceasing to be authorised for the costs that it would have been liable to pay had the FSCS made a levy in the financial year it ceased to be a participant in the scheme.

The FSCS has borrowed from HM Treasury to fund compensation costs associated with the failure of Bradford & Bingley, Heritable Bank, Kaupthing Singer & Friedlander, Landsbanki 'Icesave' and London Scottish Bank plc. The interest rate on these borrowings is subject to a floor being the higher of 12 month LIBOR plus 100 basis points or the relevant gilt rate for the equivalent cost of borrowing from HMT. The FSCS and HM Treasury have agreed that the period of these loans will reflect the expected timetable for recoveries from the estates of Bradford & Bingley and the other failed banks. The FSCS will levy the deposit taking sector for its share of the balance of the principal outstanding for the non-Bradford & Bingley loan prior to the FSCS loan facility with HMT expiring in March 2016. In addition, the FSCS levied an interim payment relating to resolution costs for Dunfermline Building Society of £100 million. The capital element levied on the industry in 2014/15 scheme year was £399 million (£363 million in the 2013/14 scheme year).

The Group has accrued £110 million for its share of estimated FSCS levies.

Litigation, investigations and reviews

RBS plc and other members of the RBS Group are party to legal proceedings and the subject of investigation and other regulatory and governmental action ("Matters") in the United Kingdom (UK), the United States (US), the European Union (EU) and other jurisdictions.

The RBS Group recognises a provision for a liability in relation to these Matters when it is probable that an outflow of economic benefits will be required to settle an obligation resulting from past events, and a reliable estimate can be made of the amount of the obligation. While the outcome of these Matters is inherently uncertain, the directors believe that, based on the information available to them, appropriate provisions have been made in respect of the Matters as at 31 December 2015 (see Note 21). The aggregate provisions for regulatory and legal actions of £2.9 billion recognised during 2015 mainly included provisions in respect of mortgage backed securities litigation (£2.1 billion).

In many proceedings and investigations, it is not possible to determine whether any loss is probable or to estimate reliably the amount of any loss, either as a direct consequence of the relevant proceedings and investigations or as a result of adverse impacts or restrictions on the RBS Group's reputation, businesses and operations. Numerous legal and factual issues may need to be resolved, including through potentially lengthy discovery and document production exercises and determination of important factual matters, and by addressing novel or unsettled legal questions relevant to the proceedings in question, before a liability can reasonably be estimated for any claim. The RBS Group cannot predict if, how, or when such claims will be resolved or what the eventual settlement, damages, fine, penalty or other relief, if any, may be, particularly for claims that are at an early stage in their development or where claimants seek substantial or indeterminate damages.

In respect of certain matters described below, we have established a provision and in certain of those matters, we have indicated that we have established a provision.

There are situations where the RBS Group may pursue an approach that in some instances leads to a settlement agreement. This may occur in order to avoid the expense, management distraction or reputational implications of continuing to contest liability, or in order to take account of the risks inherent in defending claims or investigations even for those matters for which the RBS Group believes it has credible defences and should prevail on the merits. The uncertainties inherent in all such matters affect the amount and timing of any potential outflows for both matters with respect to which provisions have been established and other contingent liabilities.

The future outflow of resources in respect of any matter may ultimately prove to be substantially greater than or less than the aggregate provision that the RBS Group has recognised. Where (and as far as) liability cannot be reasonably estimated, no provision has been recognised.

Other than those discussed below, no member of the Group is or has been involved in governmental, legal or regulatory proceedings (including those which are pending or threatened) that are expected to be material, individually or in aggregate. The RBS Group expects that in future periods additional provisions, settlement amounts, and customer redress payments will be necessary, in amounts that are expected to be substantial in some instances.

Litigation

Shareholder litigation (UK)

Between March and July 2013, claims were issued in the High Court of Justice of England and Wales by sets of current and former shareholders, against the RBS Group (and in one of those claims, also against certain former individual officers and directors) alleging that untrue and misleading statements and/or improper omissions, in breach of the Financial Services and Markets Act 2000, were made in connection with the rights issue announced by the RBS Group on 22 April 2008. In July 2013 these and other similar threatened claims were consolidated by the Court via a Group Litigation Order. The RBS Group's defence to the claims was filed on 13 December 2013. Since then, further High Court claims have been issued against the RBS Group under the Group Litigation Order which is now closed to further claimants. The aggregate value of the shares subscribed for at 200 pence per share by the claimant shareholders is approximately £4 billion although their damages claims are not yet quantified.

The court timetable provides that a trial of the preliminary issue of whether the rights issue prospectus contained untrue and misleading statements and/or improper omissions will commence in March 2017. In the event that the court makes such a finding, further trial(s) will be required to consider whether any such statements and/or omissions caused loss and, if so, the quantum of that loss.

Other securitisation and securities related litigation in the US

RBS Group companies have been named as defendants in their various roles as issuer, depositor and/or underwriter in a number of claims in the US that relate to the securitisation and securities underwriting businesses. These cases include actions by individual purchasers of securities and a purported class action suit. Together, the pending individual and class action cases (including those claims specifically described in this note) involve the issuance of approximately US$42 billion of mortgage-backed securities (MBS) issued primarily from 2005 to 2007.

In general, plaintiffs in these actions claim that certain disclosures made in connection with the relevant offerings contained materially false or misleading statements and/or omissions regarding the underwriting standards pursuant to which the mortgage loans underlying the securities were issued.

RBS Group companies remain as defendants in more than 20 lawsuits brought by or on behalf of purchasers of MBS, including the purported class action identified below.

Litigation, investigations and reviews (continued)

In the event of an adverse judgment in any of these cases, the amount of the RBS Group's liability will depend on numerous factors that are relevant to the calculation of damages, which may include the recognised loss of principal value in the securities at the time of judgment (write-downs); the value of the remaining unpaid principal balance of the securities at the time the case began, at the time of judgment (if the plaintiff still owns the securities at the time of judgment), or at the time when the plaintiff disposed of the securities (if plaintiff sold the securities); and a calculation of pre and post judgment interest that the plaintiff could be awarded, which could be a material amount.

In September 2011, the US Federal Housing Finance Agency (FHFA) as conservator for the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) filed MBS-related lawsuits against the RBS Group and a number of other financial institutions, all of which, except for the two cases described below, have since settled for amounts that were publicly disclosed.

The primary FHFA lawsuit against the RBS Group remains pending in the United States District Court for the District of Connecticut, and it relates to approximately US$32 billion of MBS for which RBS Group entities acted as sponsor/depositor and/or lead underwriter or co-lead underwriter. Of these US$32 billion, approximately US$8.6 billion were outstanding at 31 December 2015 with cumulative write downs to date on the securities of approximately US$1.1 billion (being the recognised loss of principal value suffered by security holders). In September 2013, the Court denied the defendants' motion to dismiss FHFA's amended complaint in this case. This matter continues in the discovery phase.

The other remaining FHFA lawsuit that involves the RBS Group relates to MBS issued by Nomura Holding America Inc. (Nomura) and subsidiaries and is now the subject of an appeal. On 11 May 2015, following a trial, the United States District Court for the Southern District of New York issued a written decision in favour of FHFA on its claims against Nomura and RBS Securities Inc., finding, as relevant to the RBS Group, that the offering documents for four Nomura-issued MBS for which RBS Securities Inc. served as an underwriter, relating to US$1.4 billion in original principal balance, contained materially misleading statements about the mortgage loans that backed the securitisations, in violation of the Securities Act and Virginia securities law.

RBS Securities Inc. estimates that its net exposure under the Court's judgment is approximately US$383 million, which consists of the difference between the amount of the judgment against RBS Securities Inc. (US$636 million) and the current estimated market value of the four MBS that FHFA would return to RBS Securities Inc. pursuant to the judgment, plus the costs and attorney's fees that will be due to FHFA if the judgment is upheld.

The Court has stayed the judgment pending the result of the appeal that the defendants are taking to the United States Court of Appeals for the Second Circuit, though post-judgment interest on the judgment amount will accrue while the appeal is pending. RBS Securities Inc. intends to pursue a contractual claim for indemnification against Nomura with respect to any losses it suffers as a result of this matter.

The National Credit Union Administration Board (NCUA) is litigating two MBS cases against RBS Group companies (on behalf of US Central Federal Credit Union and Western Corporate Federal Credit Union). The original principal balance of the MBS at issue in these two NCUA cases is US$3.25 billion. In September 2015, in a third case brought by NCUA (on behalf of Southwest Corporate Federal Credit Union and Members United Corporate Federal Credit Union), the NCUA accepted RBS's offer of judgment for US$129.6 million, plus attorney's fees, to resolve the matter, which concerned US$312 million in MBS. RBS has paid to the plaintiff the agreed US$129.6 million plus attorney's fees.

Other remaining MBS lawsuits against RBS Group companies include, among others, cases filed by the Federal Home Loan Banks of Boston and Seattle. RBS has settled the MBS lawsuits filed by the Federal Home Loan Bank of San Francisco and the Commonwealth of Virginia on behalf of the Virginia Retirement System for amounts that have now been provided for or paid to the plaintiffs.

RBS Group companies are also defendants in a purported MBS class action entitled New Jersey Carpenters Health Fund v. Novastar Mortgage Inc. et al., which remains pending in the United States District Court for the Southern District of New York. Another MBS class action (Luther v. Countrywide Financial Corp. et al. and related class action cases) was settled in 2013 without any contribution from the RBS Group, but several members of the settlement class are appealing the court-approved settlement to the United States Court of Appeals for the Ninth Circuit.

Certain other claims on behalf of public and private institutional investors have been threatened against the RBS Group in connection with various mortgage-related offerings. The RBS Group cannot predict whether any of these threatened claims will be pursued, but expects that several may.

The RBS Group has £3.8 billion in cumulative provisions relating to the MBS litigation described in this note, including £2.1 billion added in 2015. Additional settlement costs or provisions related to the MBS litigation, as well as the investigations into MBS-related conduct involving the RBS Group set out under 'Investigations and reviews' on page 237 (for which no provisions have been made), may be necessary in future periods for amounts that could be substantial in some instances and in aggregate could be substantially in excess of the £3.8 billion in existing provisions.

Litigation, investigations and reviews (continued)

In many of the securitisation and securities related cases in the US, the RBS Group has or will have contractual claims to indemnification from the issuers of the securities (where an RBS Group company is underwriter) and/or the underlying mortgage originator (where an RBS Group company is issuer). The amount and extent of any recovery on an indemnification claim, however, is uncertain and subject to a number of factors, including the ongoing creditworthiness of the indemnifying party a number of whom are or may be insolvent.

London Interbank Offered Rate (LIBOR)

Certain members of the RBS Group have been named as defendants in a number of class actions and individual claims filed in the US with respect to the setting of LIBOR and certain other benchmark interest rates. The complaints are substantially similar and allege that certain members of the RBS Group and other panel banks individually and collectively violated various federal laws, including the US commodities and antitrust laws, and state statutory and common law, as well as contracts, by manipulating LIBOR and prices of LIBOR-based derivatives in various markets through various means.

Most of the USD LIBOR-related actions in which RBS Group companies are defendants, including all purported class actions relating to USD LIBOR, were transferred to a coordinated proceeding in the United States District Court for the Southern District of New York.

In the coordinated proceeding, consolidated class action complaints were filed on behalf of (1) exchange-based purchaser plaintiffs, (2) over-the-counter purchaser plaintiffs, and (3) corporate debt purchaser plaintiffs. Over 35 other USD LIBOR-related actions naming RBS Group companies as defendants, including purported class actions on behalf of lenders and mortgage borrowers, were also made part of the coordinated proceeding.

In a series of orders issued in 2013 and 2014, the Court overseeing the coordinated USD proceeding dismissed class plaintiffs' antitrust claims and claims under RICO (Racketeer Influenced and Corrupt Organizations Act), but declined to dismiss (a) certain Commodity Exchange Act claims on behalf of persons who transacted in Eurodollar futures contracts and options on futures contracts on the Chicago Mercantile Exchange (on the theory that defendants' alleged persistent suppression of USD LIBOR caused loss to plaintiffs), and (b) certain contract and unjust enrichment claims on behalf of over-the-counter purchaser plaintiffs who transacted directly with a defendant. Since then, the Court has issued additional orders broadly addressing other potential grounds for dismissal of various of plaintiffs' claims, including dismissal for lack of personal jurisdiction, and the Court is now in the process of applying these rulings across the cases in the coordinated proceeding. The Court's dismissal of plaintiffs' antitrust claims is currently on appeal to the United States Court of Appeals for the Second Circuit.

Certain members of the RBS Group have also been named as defendants in class actions relating to (i) JPY LIBOR and Euroyen TIBOR, (ii) Euribor, (iii) Swiss Franc LIBOR, and (iv) Pound sterling LIBOR, all of which are pending before other judges in the United States District Court for the Southern District of New York. On 28 March 2014, the Court in the action relating to Euroyen TIBOR futures contracts dismissed the plaintiffs' antitrust claims, but declined to dismiss their claims under the Commodity Exchange Act for price manipulation.

Details of LIBOR investigations involving the RBS Group are set out under 'Investigations and reviews' on page 237.

ISDAFIX antitrust litigation

Beginning in September 2014, RBS plc and a number of other financial institutions were named as defendants in several purported class action complaints (now consolidated into one complaint) pending in the United States District Court for the Southern District of New York) alleging manipulation of USD ISDAFIX rates. RBS plc has reached an agreement to settle this matter, subject to final settlement documentation and court approval. The settlement amount is covered by an existing provision.

Credit default swap antitrust litigation

Certain members of the RBS Group, as well as a number of other financial institutions, are defendants in a consolidated antitrust class action pending in the United States District Court for the Southern District of New York alleging an unlawful restraint of trade in the market for credit default swaps. The RBS Group defendants have reached an agreement to settle this matter for US$33 million, and that settlement received preliminary approval from the Court on 29 October 2015. The settlement amount has been paid into escrow pending final court approval of the settlement.

FX antitrust litigation

RBS Group companies have settled all claims that are or could be asserted on behalf of the classes in a consolidated action alleging an antitrust conspiracy in relation to foreign exchange transactions, which is pending in the United States District Court for the Southern District of New York. Following the Court's preliminary approval of the settlement on 15 December 2015, the RBS Group paid the total settlement amount (US$255 million) into escrow pending final court approval of the settlement. Other class action complaints, including a complaint asserting Employee Retirement Income Security Act claims on behalf of employee benefit plans that engaged in FX transactions, are pending in the same court and name certain members of the RBS Group as defendants.

In September 2015, certain members of the RBS Group, as well as a number of other financial institutions, were named as defendants in two purported class actions filed in Ontario and Quebec on behalf of persons in Canada who entered into foreign exchange transactions or who invested in funds that entered into foreign exchange transactions. The plaintiffs allege that the defendants violated the Canadian Competition Act by conspiring to manipulate the prices of currency trades.

Litigation, investigations and reviews (continued)

Certain other foreign exchange transaction related claims have been or may be threatened against the RBS Group in other jurisdictions. The RBS Group cannot predict whether any of these claims will be pursued, but expects that several may.

US Treasury securities antitrust litigation

Beginning in July 2015, numerous class action antitrust complaints were filed in US federal courts against a number of primary dealers of US Treasury securities, including RBS Securities Inc. The complaints allege that the defendants rigged the US Treasury securities auction bidding process to deflate prices at which they bought such securities and colluded to increase the prices at which they sold such securities to plaintiffs. The complaints assert claims under the US antitrust laws and the Commodity Exchange Act on behalf of persons who transacted in US Treasury securities or derivatives based on such instruments, including futures and options. On 8 December 2015, all pending matters were transferred to the United States District Court for the Southern District of New York for coordinated or consolidated pretrial proceedings.

Interest rate swaps antitrust litigation

On 25 November 2015, RBS plc and other members of the RBS Group, as well as a number of other interest rate swap dealers, were named as defendants in a class action antitrust complaint filed in the United States District Court for the Southern District of New York. A similar complaint was filed in the United States District Court for the Northern District of Illinois on 18 February 2016. The complaints allege that the defendants violated the US antitrust laws by restraining competition in the market for interest rate swaps through various means and thereby caused inflated bid-ask spreads for interest rate swaps, to the alleged detriment of the plaintiff class. The RBS Group companies named as defendants anticipate moving to dismiss the claims asserted in these matters.

Thornburg adversary proceeding

RBS Securities Inc. and certain other RBS Group companies, as well as several other financial institutions, are defendants in an adversary proceeding filed in the US bankruptcy court in Maryland by the trustee for TMST, Inc. (formerly known as Thornburg Mortgage, Inc.). The trustee seeks recovery of transfers made under certain restructuring agreements as, among other things, avoidable fraudulent and preferential conveyances and transfers. On 25 September 2014, the Court largely denied the defendants' motion to dismiss this matter and, as a result, discovery is ongoing.

Interest rate hedging products litigation

The RBS Group is dealing with a large number of active litigation claims in relation to the sale of interest rate hedging products (IRHPs). In general claimants allege that the relevant interest rate hedging products were mis-sold to them, with some also alleging the RBS Group made misrepresentations in relation to LIBOR. Claims have been brought by customers who were considered under the UK Financial Conduct Authority (FCA) redress programme, as well as customers who were outside of the scope of that programme, which was closed to new entrants on 31 March 2015.

The RBS Group encouraged those customers that were eligible to seek redress under the FCA redress programme to participate in that programme. The RBS Group remains exposed to potential claims from customers who were either ineligible to be considered for redress or who are dissatisfied with their redress offers.

In addition to claims alleging that IRHPs were mis-sold, the RBS Group has received a number of claims involving allegations that it breached a legal duty of care in its conduct of the FCA redress programme. These claims have been brought by customers who are dissatisfied with redress offers made to them through the FCA redress programme. The claims followed a preliminary decision against another UK bank. RBS has since been successful in opposing an application by a customer to amend its pleadings to include similar claims against RBS, on the basis that the bank does not owe a legal duty of care to customers in carrying out the FCA review. The customer was declined permission to appeal by the Mercantile Court and has formally applied to the Court of Appeal for leave to appeal.

Weiss v. National Westminster Bank Plc

National Westminster Bank Plc (NatWest) is defending a lawsuit filed by a number of US nationals (or their estates, survivors, or heirs) who were victims of terrorist attacks in Israel. The plaintiffs allege that NatWest is liable for damages arising from those attacks pursuant to the US Anti-terrorism Act because NatWest previously maintained bank accounts and transferred funds for the Palestine Relief & Development Fund, an organisation which plaintiffs allege solicited funds for Hamas, the alleged perpetrator of the attacks. On 28 March 2013, the trial court (the United States District Court for the Eastern District of New York) granted summary judgment in favour of NatWest on the issue of scienter, but on 22 September 2014, that summary judgment ruling was vacated by the United States Court of Appeals for the Second Circuit. The appeals court returned the case to the trial court for consideration of NatWest's other asserted grounds for summary judgment and, if necessary, for trial.

Investigations and reviews

The Group's businesses and financial condition can be affected by the actions of various governmental and regulatory authorities in the UK, the EU, the US and elsewhere. The RBS Group has engaged, and will continue to engage, in discussions with relevant governmental and regulatory authorities, including in the UK, the US, the EU and elsewhere, on an ongoing and regular basis, and in response to informal and formal inquiries or investigations, regarding operational, systems and control evaluations and issues including those related to compliance with applicable laws and regulations, including consumer protection, business conduct, competition, anti-trust, anti-bribery, anti-money laundering and sanctions regimes. The Corporate & Institutional Banking (CIB) segment in particular has been providing information regarding a variety of matters, including, for example, the setting of benchmark rates and related derivatives trading, conduct in the foreign exchange market, and various issues relating to the issuance, underwriting, and sales and trading of fixed-income securities, including structured products and government securities.

Litigation, investigations and reviews (continued)

Any matters discussed or identified during such discussions and inquiries may result in, among other things, further inquiry or investigation, other action being taken by governmental and regulatory authorities, increased costs being incurred by the RBS Group, remediation of systems and controls, public or private censure, restriction of the RBS Group's business activities and/or fines. Any of the events or circumstances mentioned in this paragraph or below could have a material adverse effect on the RBS Group, its business, authorisations and licences, reputation, results of operations or the price of securities issued by it.

The RBS Group is co-operating fully with the investigations and reviews described below.

Loan securitisation business investigations

In the US, the RBS Group is involved in reviews, investigations and proceedings (both formal and informal) by federal and state governmental law enforcement and other agencies and self-regulatory organisations, including the DOJ and various other members of the RMBS Working Group of the Financial Fraud Enforcement Task Force (including several state attorneys general), relating to, among other things, issuance, underwriting and trading in mortgage-backed securities, collateralised debt obligations (CDOs), collateralised loan obligations (CLOs) and synthetic products.

In connection with these inquiries, RBS Group companies have received requests for information and subpoenas seeking information about, among other things, the structuring of CDOs, financing to loan originators, purchase of whole loans, sponsorship and underwriting of securitisations, due diligence, representations and warranties, communications with ratings agencies, disclosure to investors, document deficiencies, trading activities and practices and repurchase requests.

These ongoing matters include, among others, active investigations by the civil and criminal divisions of the DOJ and the office of the attorney general of Connecticut, on behalf of the Connecticut Department of Banking, relating primarily to due diligence on and disclosure related to loans purchased for, or otherwise included in, securitisations and related disclosures. On 31 August 2015, the Connecticut Department of Banking issued two letters to RBS Securities Inc., indicating that it is has concluded that RBS Securities Inc. may have violated the Connecticut Uniform Securities Act when underwriting MBS, noting RBS plc's May 2015 FX-related guilty plea, and offering an opportunity for RBS Securities Inc. to demonstrate its compliance with the law and why administrative proceedings seeking fines and other remedies should not be commenced.

RBS Securities Inc. submitted responses to these letters in October 2015, and related discussions are ongoing.

The investigations also include civil and criminal investigations relating to alleged misrepresentations in the trading of various forms of asset-backed securities, including residential mortgage-backed securities, commercial mortgage-backed securities, CDOs, and CLOs. In March and December 2015, two former RBS Securities Inc. traders entered guilty pleas in the United States District Court for the District of Connecticut, each to one count of conspiracy to commit securities fraud while employed at RBS Securities Inc.

In 2007, the New York State Attorney General issued subpoenas to a wide array of participants in the securitisation and securities industry, focusing on the information underwriters obtained from the independent firms hired to perform due diligence on mortgages. The RBS Group completed its production of documents requested by the New York State Attorney General in 2008, principally producing documents related to loans that were pooled into one securitisation transaction.

In May 2011, the New York State Attorney General requested additional information about the RBS Group's mortgage securitisation business and, following the formation of the RMBS Working Group, has focused on the same or similar issues as the other state and federal RMBS Working Group investigations described above. The investigation is ongoing and the RBS Group continues to respond to requests for information.

At this stage, as there remains considerable uncertainty around the outcome of MBS-related regulatory and governmental investigations it is not practicable reliably to estimate the aggregate potential impact on the RBS Group which is expected to be material.

US mortgages - loan repurchase matters

The RBS Group's CIB business in North America has been a purchaser of non-agency US residential mortgages in the secondary market, and an issuer and underwriter of non-agency residential mortgage-backed securities (MBS). CIB did not originate or service any US residential mortgages and it was not a significant seller of mortgage loans to government sponsored enterprises (GSEs) (e.g. the Federal National Mortgage Association and the Federal Home Loan Mortgage Association).

In issuing MBS, CIB generally assigned certain representations and warranties regarding the characteristics of the underlying loans made by the originator of the residential mortgages; however, in some circumstances, CIB made such representations and warranties itself. Where CIB has given those or other representations and warranties (whether relating to underlying loans or otherwise), CIB may be contractually required to repurchase such loans or indemnify certain parties against losses for certain breaches of such representations and warranties.

Litigation, investigations and reviews (continued)

In certain instances where it is required to repurchase loans or related securities, CIB may be able to assert claims against third parties who provided representations or warranties to CIB when selling loans to it, although the ability to recover against such parties is uncertain. Between the start of 2009 and 31 December 2015, CIB received approximately US$753 million in repurchase demands in respect of loans made primarily from 2005 to 2008 and related securities sold where obligations in respect of contractual representations or warranties were undertaken by CIB. However, repurchase demands presented to CIB are subject to challenge and rebuttal by CIB.

At this stage, as there remains considerable uncertainty around the outcome of loan repurchase related claims it is not practicable reliably to estimate the aggregate potential impact, if any, on the RBS Group which may be material.

LIBOR and other trading rates

In February 2013, the RBS Group announced settlements with the Financial Services Authority (FSA) in the UK, the United States Commodity Futures Trading Commission (CFTC) and the United States Department of Justice (DOJ) in relation to investigations into submissions, communications and procedures around the setting of LIBOR. The RBS Group agreed to pay penalties of £87.5 million, US$325 million and US$150 million to these authorities respectively to resolve the investigations and also agreed to certain undertakings in its settlement with the CFTC. As part of the agreement with the DOJ, RBS plc entered into a Deferred Prosecution Agreement (DPA) in relation to one count of wire fraud relating to Swiss Franc LIBOR and one count for an antitrust violation relating to Yen LIBOR. The DPA expired in April 2015 and is of no further effect.

In April 2013, RBS Securities Japan Limited entered a plea of guilty to one count of wire fraud relating to Yen LIBOR and in January 2014, the US District Court for the District of Connecticut entered a final judgment in relation to the conviction of RBS Securities Japan Limited pursuant to the plea agreement.

In February 2014, the RBS Group paid settlement penalties of approximately €260 million and €131 million to resolve investigations by the European Commission (EC) into Yen LIBOR competition infringements and EURIBOR competition infringements respectively. This matter is now concluded.

In July 2014, RBS plc and RBS N.V. entered into an Enforceable Undertaking with the Australian Securities and Investments Commission (ASIC) in relation to potential misconduct involving the Australian Bank Bill Swap Rate. RBS plc and RBS N.V. made various undertakings and agreed to make a voluntary contribution of A$1.6 million to fund independent financial literacy projects in Australia.

In October 2014, the EC announced its findings that (1) the RBS Group and one other financial institution had participated in a bilateral cartel aimed at influencing the Swiss Franc LIBOR benchmark interest rate between March 2008 and July 2009; and (2) the RBS Group and three other financial institutions had participated in a related cartel on bid-ask spreads of Swiss Franc interest rate derivatives in the European Economic Area (EEA). The RBS Group received full immunity from fines.

The RBS Group is co-operating with investigations and new and ongoing requests for information by various other governmental and regulatory authorities, including in the UK, US and Asia, into its submissions, communications and procedures relating to a number of trading rates, including LIBOR and other interest rate settings, and non-deliverable forwards.

The RBS Group is providing information and documents to the CFTC as part of its investigation into the setting of USD, EUR and GBP ISDAFIX and related trading activities. The RBS Group understands that the CFTC investigation is at an advanced stage. The RBS Group is also under investigation by competition authorities in a number of jurisdictions stemming from the actions of certain individuals in the setting of LIBOR and other trading rates, as well as interest rate-related trading. At this stage, as there remains considerable uncertainty around the outcome of these investigations, it is not practicable to estimate the aggregate impact reliably, if any, on the RBS Group which may be material.

Foreign exchange related investigations

In November 2014, RBS plc reached a settlement with the FCA and the CFTC in relation to investigations into failings in RBSG's FX businesses within its Corporate & Institutional Banking (CIB) segment. RBS plc agreed to pay penalties of £217 million to the FCA and US$290 million to the CFTC to resolve the investigations. The fines were paid on 19 November 2014.

On 20 May 2015, RBS plc announced that it had reached settlements with the DOJ and the Board of Governors of the Federal Reserve System (Federal Reserve) in relation to investigations into its FX business within its CIB segment. RBS plc paid a penalty of US$274 million to the Federal Reserve and has agreed to pay a penalty of US$395 million to the DOJ to resolve the investigations. The DOJ fine is fully covered by existing provisions.

As part of its plea agreement with the DOJ, RBS plc pled guilty in the United States District Court for the District of Connecticut to a one-count information charging an antitrust conspiracy. RBS plc admitted that it knowingly, through one of its euro/US dollar currency traders, joined and participated in a conspiracy to eliminate competition in the purchase and sale of the euro/US dollar currency pair exchanged in the FX spot market.

The charged conspiracy occurred between as early as December 2007 to at least April 2010. Pursuant to the plea agreement (which is publicly available), the DOJ and RBS plc have agreed jointly to recommend to the Court that it impose a sentence consisting of a US$395 million criminal fine and a term of probation, which among other things, would prohibit RBS plc from committing another crime in violation of US law or engaging in the FX trading practices that form the basis for the charged crime and require RBS plc to implement a compliance program designed to prevent and detect the unlawful conduct at issue and to strengthen its compliance and internal controls as required by other regulators (including the FCA and the CFTC). If RBS plc is sentenced to a term of probation, a violation of the terms of probation could lead to the imposition of additional penalties.

Litigation, investigations and reviews (continued)

RBS plc and RBS Securities Inc. have also entered into a cease and desist order with the Federal Reserve relating to FX and other designated market activities (the FX Order). In the FX Order, which is publicly available and will remain in effect until terminated by the Federal Reserve, RBS plc and RBS Securities Inc. agreed to take certain remedial actions with respect to FX activities and certain other designated market activities, including the creation of an enhanced written internal controls and compliance program, an improved compliance risk management program, and an enhanced internal audit program. RBS plc and RBS Securities Inc. are obligated to implement and comply with these programs after they are approved by the Federal Reserve, and are also required to conduct, on an annual basis, a review of applicable compliance policies and procedures and a risk-focused sampling of key controls.

The RBS Group is responding to investigations and inquiries from other governmental and regulatory (including competition) authorities on similar issues relating to failings in its FX business within its CIB segment, including with respect to potential collateral consequences of the RBS plc guilty plea described above. The timing and amount of financial penalties with respect to any further settlements and related litigation risks and collateral consequences remain uncertain and could be material.

On 21 July 2014, the Serious Fraud Office in the UK (SFO) announced that it was launching a criminal investigation into allegations of fraudulent conduct in the foreign exchange market, apparently involving multiple financial institutions. On 15 March 2016, the SFO announced that it was closing its investigation, having concluded that, based on the information and material obtained, there was insufficient evidence for a realistic prospect of conviction.

Interest rate hedging products (IRHP) redress programme

In June 2012, following an industry wide review, the FSA announced that the RBS Group and other UK banks had agreed to a redress exercise and past business review in relation to the sale of interest rate hedging products to some small and medium sized businesses classified as retail clients or private customers under FSA rules.

In January 2013, the FSA issued a report outlining the principles to which it wished the RBS Group and other UK banks to adhere in conducting the review and redress exercise. This exercise is being scrutinised by an independent reviewer, KPMG (appointed as a Skilled Person under section 166 of the Financial Services and Markets Act), who is reviewing and approving all outcomes, and the FCA is overseeing this. The RBS Group has reached agreement with KPMG in relation to redress determinations for all in scope customers. The review and redress exercise was closed to new entrants on 31 March 2015. RBS and KPMG are now focussing on securing the few remaining acceptances of redress offers and assessing consequential loss claims. In October 2015, RBS agreed with the FCA that its review was nearing completion, and on 31 October 2015 all customers who had received final redress offers but had not yet responded were informed that the final date for acceptance of those offers was 31 January 2016.

Customers who have not yet received a final redress determination will be given three months to accept any redress offer before that offer lapses. As at the end of February 2016, 95% of all review files had been closed.

The Central Bank of Ireland also requested Ulster Bank Ireland Limited (UBIL), along with a number of Irish banks, to undertake a similar exercise and past business review in relation to the sale of IRHP to retail designated small and medium sized businesses in the Republic of Ireland. The RBS Group also agreed to undertake a similar exercise and past business review in respect of relevant customers of RBS International. The reviews undertaken in respect of both RBS International customers and UBIL customers are complete.

The RBS Group provisions in relation to the above redress exercises total £1.5 billion to date for these matters, of which £1.4 billion had been utilised at 31 December 2015.

Judicial Review of Skilled Person's role in IRHP review

RBS plc and NatWest have been named as interested parties in a number of claims for judicial review of KPMG's decisions as Skilled Person in the RBS Group's previously disclosed IRHP redress programme. This follows a similar claim from a customer of another UK bank, also against KPMG.

All of these claims were stayed pending the outcome of the other bank's case. The trial in that case was heard on 25 January 2016. The court decided in favour of KPMG, finding that (1) KPMG is not a body amenable to judicial review in respect of its role as Skilled Person in this matter; and (2) that there was no unfairness by the other bank in the procedure adopted. The claimant has sought permission to appeal the decision.

If permission to appeal is granted and the appeal court finds that a section 166-appointed Skilled Person is susceptible to judicial review, the claims against RBS plc and NatWest may then proceed to full hearing to assess the fairness of KPMG's role in the redress programme in those particular cases. If deemed unfair, this could have a consequential impact on the reasonableness of the methodology applied to reviewed and settled IRHP files generally.

As there remains some uncertainty, it is not practicable reliably to estimate the impact of this matter, if any, on the Group which may be material.

FSA mystery shopping review

In February 2013, the FSA announced the results of a mystery shopping review it undertook into the investment advice offered by banks and building societies to retail clients. As a result of that review the FSA announced that firms involved were cooperative and agreed to take immediate action. The RBS Group was one of the firms involved.

The action required included a review of the training provided to advisers, considering whether changes are necessary to advice processes and controls for new business, and undertaking a past business review to identify any historic poor advice (and where breaches of regulatory requirements are identified, to put this right for customers).

Litigation, investigations and reviews (continued)

Subsequent to the FSA announcing the results of its mystery shopping review, the FCA has required the RBS Group to carry out a past business review and customer contact exercise on a sample of historic customers that received investment advice on certain lump sum products through the UK Financial Planning channel of the Personal & Business Banking (PBB) segment of the RBS Group, which includes RBS plc and NatWest, during the period from March 2012 until December 2012.

This review was conducted under section 166 of the Financial Services and Markets Act, under which a Skilled Person was appointed to carry out the exercise. Redress has been paid/offered to certain customers in this sample group. Following discussions with the FCA after issue of the draft section 166 report, the RBS Group agreed with the FCA that it would carry out a wider review/remediation exercise relating to certain investment, insurance and pension sales from 1 January 2011 to present. The RBS Group will be writing to the relevant customers during 2016. In addition, the RBS Group agreed with the FCA that it would carry out a remediation exercise for a specific customer segment who were sold a particular structured product, in response to concerns raised by the FCA with regard to (a) the target market for the product and (b) how the product may have been described to customers by certain advisers. Redress has been paid / offered to certain customers who took out the structured product.

The Group provisions in relation to investment advice total £187 million to date for these matters, of which £72 million had been utilised at 31 December 2015.

Card Protection Plan Limited

In August 2013, the FCA announced that Card Protection Plan Limited and 13 banks and credit card issuers, including the RBS Group, had agreed to a compensation scheme in relation to the sale of card and/or identity protection insurance to certain retail customers. The closing date before which any claims under the compensation scheme must have been submitted has now passed. All compensation payments have now been made and all claims, whether through the courts or the Financial Ombudsman Service, are now barred. The compensation payments were covered by existing provisions.

Packaged accounts

As a result of an uplift in packaged current account complaints, the Group proactively put in place dedicated resources in 2013 to investigate and resolve complaints on an individual basis. The Group has made provisions totalling £307 million to date for this matter.

FCA review of the RBS Group's treatment of SMEs

In November 2013, a report by Lawrence Tomlinson, entrepreneur in residence at the UK Government's Department for Business Innovation and Skills, was published ("Tomlinson Report"). The Tomlinson Report was critical of the RBS Group's treatment of SMEs.

The Tomlinson Report was passed to the PRA and FCA. Shortly thereafter, the FCA announced that an independent Skilled Person would be appointed under section 166 of the Financial Services and Markets Act to review the allegations in the Tomlinson Report. On 17 January 2014, a Skilled Person was appointed. The Skilled Person's review is focused on the RBS Group's UK small and medium sized business customers with credit exposures of up to £20 million whose relationship was managed within the RBS Group's Global Restructuring Group or within similar units within the RBS Group's Corporate Banking Division that were focused on customers in financial difficulties. In the period 2008 to 2013 the RBS Group was one of the leading providers of credit to the UK SME sector.

Separately, in November 2013 the RBS Group instructed the law firm Clifford Chance to conduct an independent review of the principal allegation made in the Tomlinson Report: the RBS Group was alleged to be culpable of systematic and institutional behaviour in artificially distressing otherwise viable businesses and through that putting businesses into insolvency. Clifford Chance published its report on 17 April 2014 and, while they made certain recommendations to enhance customer experience and transparency of pricing, they concluded that there was no evidence to support the principal allegation.

A separate independent review of the principal allegation, led by Mason Hayes & Curran, Solicitors, was conducted in the Republic of Ireland. The report was published in December 2014 and found no evidence to support the principal allegation.

RBS is co-operating fully with the FCA in its review.

The Skilled Person review focuses on the allegations made in the Tomlinson Report and certain observations made by Sir Andrew Large in his 2013 Independent Lending Review, and is broader in scope than the reviews undertaken by Clifford Chance and Mason, Hayes & Curran which are referred to above. The Skilled Person is expected to deliver the initial findings from its review to the RBS Group and the FCA during the first half of 2016 but no final timescale has been determined. The RBS Group will have an opportunity to respond to any such review findings before the Skilled Person delivers its final report. In the event that the Skilled Person's review concludes that there were material failings in the RBS Group's treatment of SME customers those conclusions could, depending on their nature, scale and type, result in the commencement of regulatory enforcement action by the FCA, the imposition of redress requirements and the commencement of litigation claims against the RBS Group, as well as potentially wider investigations and litigation related to the RBS Group's treatment of customers in financial difficulty. At this stage, as there remains considerable uncertainty around the final conclusions of the Skilled Person's review and any collateral consequences thereof, it is not practicable reliably to estimate the potential impact on the RBS Group.

Litigation, investigations and reviews (continued)

Multilateral interchange fees

On 11 September 2014, the Court of Justice upheld earlier decisions by the EU Commission and the General Court that MasterCard's multilateral interchange fee (MIF) arrangements for cross border payment card transactions with MasterCard and Maestro branded consumer credit and debit cards in the EEA are in breach of competition law.

In April 2013, the EC announced it was opening a new investigation into interchange fees payable in respect of payments made in the EEA by MasterCard cardholders from non-EEA countries.

In May 2013, the EC announced it had reached an agreement with Visa regarding immediate cross border credit card MIF rates. This agreement has now been market tested and was made legally binding on 26 February 2014. The agreement is to last for four years.

In addition, on 8 June 2015, a regulation on interchange fees for card payments entered into force. The regulation requires the capping of both cross-border and domestic MIF rates for debit and credit consumer cards. The regulation also sets out other reforms including to the Honour All Cards Rule which require merchants to accept all cards with the same level of MIF but not cards with different MIF levels.

In the UK, the Office of Fair Trading (OFT) had previously opened investigations into domestic interchange fees applicable in respect of Visa and MasterCard consumer and commercial credit and debit card transactions. On 6 May 2015, the successor body to the OFT, the Competition & Markets Authority (CMA), announced that it had closed these investigations on the grounds of administrative priorities.

There remains uncertainty around the outcomes of the ongoing EC investigation, and regulation, but they may have a material adverse effect on the structure and operation of four party card payment schemes in general and, therefore, on the RBS Group's business in this sector.

Payment Protection Insurance (PPI)

Since 2011, the RBS Group has been implementing a policy statement agreed with the FCA for the handling of complaints about the mis-selling of PPI. The RBS Group is also monitoring developments following the UK Supreme Court's decision in the case of Plevin v Paragon Personal Finance Ltd in November 2014. That decision was that the sale of a single premium PPI policy could create an 'unfair relationship' under s.140A of the Consumer Credit Act 1974 (the 'Consumer Credit Act') because the premium contained a particularly high level of undisclosed commission.

The Financial Ombudsman Service (FOS) has confirmed on its website that unfair relationship provisions in the Consumer Credit Act and the Plevin judgment are 'potentially relevant considerations' in some of the PPI complaints referred to FOS. On 27 May 2015, the FCA announced that it was considering whether additional rules and/or guidance are required to deal with the impact of the Plevin decision on complaints about PPI generally.

On 26 November 2015, the FCA issued Consultation Paper 15/39, in which it set out proposed rules and guidance for how firms should handle PPI complaints fairly in light of the Plevin decision and how the FOS should consider relevant PPI complaints. The Consultation Paper also contains proposals for the introduction in 2018 on a date to be confirmed of a deadline for submission of PPI complaints. The RBS Group submitted its response to the Consultation Paper on 26 February 2016.

The proposals in the Consultation Paper include an FCA-led communications campaign to raise awareness of the deadline and to prompt those who intend to complain to act ahead of the deadline. If the proposals are agreed and implemented, the RBS Group expects higher claims volumes, persisting longer than previously modelled, and additional compensation payments in relation to PPI claims made as a result of the Plevin judgment.

Complaints made after the proposed 2018 deadline would lose the right to be assessed by firms or by the Financial Ombudsman Service, bringing an end to new PPI cases in 2018.

PPI complaint volumes during Q4 2015 were in line with previous trends. Actual payments made to settle PPI claims during Q4 covered the four month period from 1 September until 31 December 2015. This is in contrast to payments made during Q3, which covered the period from 1 June until 31 August 2015. This change was due to enhanced operating processes introduced in Q4 2015.

The RBS Group has made provisions totalling £4.3 billion to date for PPI claims, including £0.6 billion for 2015, of which £3.3 billion had been utilised by 31 December.

UK retail banking

In March 2014, the CMA announced that it would be undertaking an update of the OFT's 2013 personal current account (PCA) market study, in parallel with its market study into small and medium-sized enterprise (SME) banking which was announced in June 2013. In July 2014 the CMA published its preliminary findings in respect of both the PCA and SME market studies. The CMA provisionally decided to make a market investigation reference (MIR) into retail banking which would cover PCA and SME banking. On 6 November 2014, the CMA made its final decision to proceed with a MIR. On 22 October 2015 the CMA published a summary of its provisional findings and notice of possible remedies.

The CMA has provisionally concluded there are a number of competition concerns in the provision of PCAs, business current accounts and SME lending, particularly around low levels of customers searching and switching, resulting in banks not being put under enough competitive pressure, and new products and new banks not attracting customers quickly enough.

Litigation, investigations and reviews (continued)

The notice of possible remedies sets out measures to address these concerns, including measures to make it easier for customers to compare products, and requiring banks to help raise public awareness of, and confidence in, switching bank accounts. On 7 March 2016, the CMA announced that it is extending the MIR by 3 months with a revised statutory deadline of 12 August 2016. The CMA also published a supplemental notice of possible remedies which sets out four additional remedies focussed on PCA overdrafts, in addition to the remedies set out in the October 2015 notice of possible remedies. The provisional decision on remedies will now be published in May 2016.

Alongside the MIR, the CMA is also reviewing the undertakings given by certain banks following the Competition Commission's 2002 investigation into SME banking as well as the 2008 Northern Ireland PCA Banking Market Investigation Order 2008.

At this stage as there remains uncertainty around the final outcome of these reviews it is not practicable reliably to estimate the potential impact on RBS, which may be material.

FCA Wholesale Sector Competition Review

On 9 July 2014, the FCA launched a review of competition in the wholesale sector to identify any areas which may merit further investigation through an in-depth market study.

The initial review was an exploratory exercise and focused primarily on competition in wholesale securities and investment markets, and related activities such as corporate banking. It commenced with a three month consultation exercise, including a call for inputs from stakeholders. Following this consultation period, the FCA published its feedback statement on 19 February 2015 which announced that the FCA is to undertake a market study into investment and corporate banking and potentially into asset management. The terms of reference for the investment and corporate banking market study were published on 22 May 2015. The FCA is intending to publish an interim report in April 2016.

On 18 November 2015, the FCA also announced that a market study would be undertaken into asset management. The FCA intends to publish an interim report in Summer 2016 with the final report expected in early 2017.

At this stage, as there remains considerable uncertainty around the outcome of these reviews it is not practicable reliably to estimate the aggregate impact, if any, on the RBS Group which may be material.

Credit default swaps (CDS) investigation

In April 2011 the EC opened an antitrust investigation into the CDS information market to which the RBS Group was a party. In general terms, the EC raised concerns that a number of banks, Markit and ISDA may have jointly prevented exchanges from entering the CDS market. On 4 December 2015 the EC decided to close the case against the RBS Group and the other bank parties to the investigation. Markit and ISDA remain party to the investigation.

Governance and risk management consent order

In July 2011, the RBS Group agreed with the Board of Governors of the Federal Reserve System, the New York State Banking Department, the Connecticut Department of Banking, and the Illinois Department of Financial and Professional Regulation to enter into a consent Cease and Desist Order (Governance Order) (which is publicly available) to address deficiencies related to governance, risk management and compliance systems and controls in the US branches of RBS plc and RBS N.V. branches (the US Branches).

In the Governance Order, the RBS Group agreed to create the following written plans or programmes.

- a plan to strengthen board and senior management oversight of the corporate governance, management, risk management, and operations of the RBS Group's US operations on an enterprise-wide and business line basis;
- an enterprise-wide risk management programme for the RBS Group's US operations;
- a plan to oversee compliance by the RBS Group's US operations with all applicable US laws, rules, regulations, and supervisory guidance;
- a Bank Secrecy Act/anti-money laundering compliance programme for the US Branches on a consolidated basis;
- a plan to improve the US Branches' compliance with all applicable provisions of the Bank Secrecy Act and its rules and regulations as well as the requirements of Regulation K of the Federal Reserve;
- a customer due diligence programme designed to ensure reasonably the identification and timely, accurate, and complete reporting by the US Branches of all known or suspected violations of law or suspicious transactions to law enforcement and supervisory authorities, as required by applicable suspicious activity reporting laws and regulations; and
- a plan designed to enhance the US Branches' compliance with Office of Foreign Assets Control (OFAC) requirements.

The Governance Order identified specific items to be addressed, considered, and included in each proposed plan or programme. The RBS Group also agreed in the Governance Order to adopt and implement the plans and programmes after approval by the regulators, to comply fully with the plans and programmes thereafter, and to submit to the regulators periodic written progress reports regarding compliance with the Governance Order. The RBS Group has created, submitted, and adopted plans and/or programmes to address each of the areas identified above. In connection with the RBS Group's efforts to implement these plans and programmes, it has, among other things, made investments in technology, hired and trained additional personnel, and revised compliance, risk management, and other policies and procedures for the RBS Group's US operations. The RBS Group continues to test the effectiveness of the remediation efforts it has undertaken to ensure they are sustainable and meet regulators' expectations. Furthermore, the RBS Group continues to work closely with the regulators in its efforts to fulfil its obligations under the Governance Order, which will remain in effect until terminated by the regulators.

Litigation, investigations and reviews (continued)

The RBS Group may be subject to formal and informal supervisory actions and may be required by its US banking supervisors to take further actions and implement additional remedial measures with respect to these and additional matters. The RBS Group's activities in the US may be subject to significant limitations and/or conditions.

US dollar processing consent order

In December 2013 RBSG and RBS plc agreed a settlement with the Federal Reserve, the New York State Department of Financial Services (DFS), and the Office of Foreign Assets Control (OFAC) with respect to RBS plc's historical compliance with US economic sanction regulations outside the US. As part of the settlement, RBSG and RBS plc entered into a consent Cease and Desist Order with the Federal Reserve (US Dollar Processing Order), which remains in effect until terminated by the Federal Reserve. The US Dollar Processing Order (which is publicly available) indicated, among other things, that RBSG and RBS plc lacked adequate risk management and legal review policies and procedures to ensure that activities conducted outside the US comply with applicable OFAC regulations.

The RBS Group agreed to create an OFAC compliance programme to ensure compliance with OFAC regulations by the RBS Group's global business lines outside the US, and to adopt, implement, and comply with the programme. Prior to and in connection with the US Dollar Processing Order, the RBS Group has made investments in technology, hired and trained personnel, and revised compliance, risk management, and other policies and procedures.

Under the US Dollar Processing Order (as part of the OFAC compliance programme) the RBS Group was required to appoint an independent consultant to conduct an annual OFAC compliance review of compliance policies and their implementation and an appropriate risk-focused sampling of US dollar payments. The RBS Group appointed the independent consultant and their report was submitted to the authorities on 14 June 2015. The independent consultant review examined a significant number of sanctions alerts and no reportable issues were identified.

Pursuant to the US Dollar Processing Order, the authorities have requested a second annual review to be conducted by an independent consultant during the course of 2016 and the RBS Group is currently in discussions to agree the scope and timing of such review. In addition, pursuant to requirements of the US Dollar Processing Order, the RBS Group has provided the required written submissions, including quarterly updates, in a timely manner, and RBS continues to participate in a constructive dialogue with the authorities.

US/Swiss tax programme

In August 2013, the DOJ announced a programme for Swiss banks (the Programme) which provides Swiss banks with an opportunity to obtain resolution, through non-prosecution agreements or non-target letters, of the DOJ's investigations of the role that Swiss banks played in concealing the assets of US tax payers in offshore accounts (US related accounts).

In December 2013, Coutts & Co Ltd., a member of the RBS Group incorporated in Switzerland, notified the DOJ that it intended to participate in the Programme.

As required by the Programme, Coutts & Co Ltd. subsequently conducted a review of its US related accounts and presented the results of the review to the DOJ. On 23 December 2015, Coutts & Co Ltd. entered into a non-prosecution agreement (the NPA) in which Coutts & Co Ltd. paid a US$78.5 million penalty and acknowledged responsibility for certain conduct set

forth in a statement of facts accompanying the agreement. Under the NPA, which has a term of four years, Coutts & Co Ltd. is required, among other things, to provide certain information, cooperate with DOJ's investigations, and commit no U.S. federal offenses. If Coutts & Co Ltd. abides by the NPA, the DOJ will not prosecute it for certain tax-related and monetary transaction offenses in connection with US related accounts.

German prosecutor investigation into Coutts & Co Ltd

A prosecuting authority in Germany undertook an investigation into Coutts & Co Ltd in Switzerland, and current and former employees, for alleged aiding and abetting of tax evasion by certain Coutts & Co Ltd clients. Coutts & Co Ltd cooperated with the relevant authorities and on 4 December 2015 paid EUR 23.8 million to settle the investigation against it. The settlement amount was covered by an existing provision.

Review of suitability of advice provided by Coutts & Co

In 2013 the FCA conducted a thematic review of the advice processes across the UK wealth management industry. As a result of this review, Coutts & Co undertook a past business review into the suitability of investment advice provided to its clients. This review is well advanced, with the focus on Coutts & Co contacting remaining clients and offering redress in appropriate cases. The RBS Group has made appropriate provision based on its estimate of exposure arising from this review.

Enterprise Finance Guarantee Scheme

The Enterprise Finance Guarantee (EFG) scheme is a government lending initiative for small businesses with viable business proposals that lack security for conventional lending. From 2009 until the end of 2015, the RBS Group provided over £980 million of lending under the EFG scheme. The RBS Group has identified a number of instances where it has not properly explained to customers how borrower and guarantor liabilities work under the EFG scheme. There are also concerns around the eligibility of some customers to participate in the EFG scheme and around potential over or under-payment of quarterly premiums paid by customers. In January 2015, the RBS Group announced a review of all EFG loans where there is a possibility that the customer may have been disadvantaged. The review has been completed and the RBS Group is in the final stages of advising customers of their review outcome, which in some cases involves payment of redress. The RBS Group has made appropriate provision based on its estimate of exposure arising from this review.

30 Net cash flow from operating activities

	Group			Bank		
	2015 £m	2014* £m	2013* £m	2015 £m	2014 £m	2013 £m
Operating (loss)/profit before tax - continuing operations	(3,153)	2,403	(7,367)	(1,451)	(959)	8
Profit/(loss) before tax - discontinued operations	1,750	(3,258)	606	—	—	—
Decrease/(increase) in prepayments and accrued income	411	4	267	325	(110)	1,755
Interest on subordinated liabilities	1,267	1,302	1,314	1,285	1,234	1,241
Decrease in accruals and deferred income	(829)	(222)	(634)	(550)	(157)	(394)
(Recoveries)/impairment losses	(734)	(1,140)	8,449	(260)	(46)	2,536
Loans and advances written-off net of recoveries	(8,778)	(5,052)	(3,975)	(1,492)	(2,567)	(1,892)
Unwind of discount on impairment losses	(144)	(247)	(389)	(47)	(87)	(112)
(Profit)/loss on sale of property, plant and equipment	(88)	(138)	(45)	(24)	1	—
(Profit)/loss on sale of subsidiaries and associates	(1,092)	30	(179)	30	213	(64)
Profit on sale of securities	(40)	(387)	(1,035)	(40)	(317)	(905)
Charge for defined benefit pension schemes	521	463	513	20	13	11
Pension scheme curtailment and settlement gains	(65)	—	(3)	(8)	—	(3)
Cash contribution to defined benefit pension schemes	(1,059)	(1,063)	(817)	(32)	(28)	(41)
Other provisions charged net of releases	4,470	2,478	4,407	1,326	1,453	913
Other provisions utilised	(2,159)	(3,254)	(2,046)	(1,097)	(1,606)	(1,103)
Depreciation and amortisation	1,173	1,105	1,272	548	511	634
Loss/(gain) on redemption of own debt	263	(6)	(162)	—	—	(77)
Loss on reclassification to disposal groups	273	3,994	—	—	—	—
Write down of goodwill and other intangible assets	1,331	533	423	725	393	227
Write down of investment in subsidiaries	—	—	—	6,045	4,353	86
Elimination of foreign exchange differences	(1,476)	(881)	807	(170)	123	182
Other non-cash items	(1,276)	1,135	(3,227)	(445)	73	(2,763)
Net cash (outflow)/inflow from trading activities	(9,434)	(2,201)	(1,821)	4,688	2,490	239
Decrease in loans and advances to banks and customers	57,211	13,385	56,381	65,905	14,376	69,601
Decrease/(increase) in securities	13,330	8,199	27,877	8,624	(3,244)	15,425
(Increase)/decrease in other assets	(1,813)	423	(757)	330	1,160	(976)
Decrease/(increase) in derivative assets	91,499	(65,586)	155,771	94,224	(66,945)	157,032
Changes in operating assets	160,227	(43,579)	239,272	169,083	(54,653)	241,082
Decrease in deposits by banks and customers	(38,175)	(7,609)	(88,295)	(58,740)	(25,750)	(95,704)
Decrease in debt securities in issue	(16,455)	(16,119)	(23,370)	(13,382)	(14,795)	(19,879)
Increase/(decrease) in other liabilities	3,158	(4,606)	3,651	810	(946)	416
(Decrease)/increase in derivative liabilities	(95,235)	64,795	(150,145)	(97,375)	66,241	(150,838)
(Decrease)/increase in settlement balances and short positions	(2,733)	(4,799)	(62)	596	(373)	2,772
Changes in operating liabilities	(149,440)	31,662	(258,221)	(168,091)	24,377	(263,233)
Income taxes (paid)/received	(231)	(302)	(195)	(192)	135	322
Net cash inflow/(outflow) from operating activities	1,122	(14,420)	(20,965)	5,488	(27,651)	(21,590)

*Restated - refer to page 148 for further details

31 Analysis of the net investment in business interests and intangible assets

Acquisitions and disposals	Group 2015 £m	Group 2014 £m	Group 2013 £m	Bank 2015 £m	Bank 2014 £m	Bank 2013 £m
Fair value given for businesses acquired	(59)	(54)	—	—	—	—
Value recognised for business transferred from fellow subsidiary	—	—	3,911	(2)	—	4,096
Non-cash consideration	—	—	128	—	—	128
Additional and new investments in Group undertakings	—	—	—	(856)	(1,637)	(2,300)
Net (outflow)/inflow of cash in respect of purchases	(59)	(54)	4,039	(858)	(1,637)	1,924
Other assets sold	(2,301)	(2,250)	785	(2,630)	(46)	260
Repayment of investments	—	—	—	193	—	—
Non-cash consideration	—	—	3	—	—	3
Profit/(loss) on disposal	1,092	(30)	179	(30)	(213)	64
Net cash and cash equivalents disposed	1,923	8	—	—	—	—
Net inflow/(outflow) of cash in respect of disposals	714	(2,272)	967	(2,467)	(259)	327
Dividends received from associates	11	10	77	—	—	59
Cash expenditure on intangible assets	(613)	(631)	(846)	(612)	(462)	(664)
Net inflow/(outflow)	53	(2,947)	4,237	(3,937)	(2,358)	1,646

Note:
(1) Includes cash proceeds of £1,628 million in 2015 relating to the disposal of the controlling interest in Citizens and £578 million in 2013 relating to the disposal of the controlling interest in Direct Line Group.

32 Interest received and paid

	Group 2015 £m	Group 2014 £m	Group 2013 £m	Bank 2015 £m	Bank 2014 £m	Bank 2013 £m
Interest received	11,589	13,039	17,479	5,579	6,997	11,379
Interest paid	(3,699)	(4,332)	(6,387)	(3,800)	(4,140)	(7,752)
	7,890	8,707	11,092	1,779	2,857	3,627

33 Analysis of changes in financing during the year

	Group					
	Share capital, share premium and merger reserve			Subordinated liabilities		
	2015 £m	2014 £m	2013 £m	2015 £m	2014 £m	2013 £m
At 1 January	44,250	43,699	43,571	30,469	33,134	33,851
Issue of subordinated liabilities				—	1,438	2,285
Repayment of subordinated liabilities				(2,279)	(4,181)	(1,868)
Net cash (outflow)/inflow from financing	—	—	—	(2,279)	(2,743)	417
Cross-border merger	—	—	128	—	—	—
Redemption of preference shares	—	517	—	—	—	—
Currency translation and other adjustments	31	34	—	(1,160)	78	(1,134)
At 31 December	44,281	44,250	43,699	27,030	30,469	33,134

	Bank					
	Share capital, share premium and merger reserve			Subordinated liabilities		
	2015 £m	2014 £m	2013 £m	2015 £m	2014 £m	2013 £m
At 1 January	33,369	32,818	32,690	27,480	30,566	31,635
Issue of subordinated liabilities				—	833	1,864
Repayment of subordinated liabilities				(1,894)	(4,121)	(1,868)
Net cash outflow from financing	—	—	—	(1,894)	(3,288)	(4)
Cross-border merger	—	—	128	—	—	—
Redemption of preference shares	—	517	—	—	—	—
Currency translation and other adjustments	31	34	—	(52)	202	(1,065)
At 31 December	33,400	33,369	32,818	25,534	27,480	30,566

34 Analysis of cash and cash equivalents

	Group (1)			Bank (2)		
	2015 £m	2014 £m	2013 £m	2015 £m	2014 £m	2013 £m
At 1 January						
- cash	90,191	97,340	86,561	82,975	96,056	83,644
- cash equivalents	17,117	30,616	46,540	18,395	28,572	42,599
	107,308	127,956	133,101	101,370	124,628	126,243
Net cash (outflow)/inflow	(5,233)	(20,648)	(5,145)	5,243	(23,258)	(1,615)
At 31 December	102,075	107,308	127,956	106,613	101,370	124,628
Comprising:						
Cash and balances at central banks	78,999	73,983	79,993	76,904	70,952	75,792
Treasury bills and debt securities	1,445	1,821	696	1,179	739	429
Loans and advances to banks	21,631	31,504	47,267	28,530	29,679	48,407
Cash and cash equivalents	102,075	107,308	127,956	106,613	101,370	124,628

Notes:
(1) Includes cash collateral posted with bank counterparties in respect of derivative liabilities of £11,046 million (2014 - £11,258 million, 2013 - £9,672 million).
(2) Includes cash collateral posted with bank counterparties in respect of derivative liabilities of £10,843 million (2014 - £10,845 million, 2013 - £9,050 million).

Certain members of the Group are required by law or regulation to maintain balances with the central banks in the jurisdictions in which they operate. These balances are set out below.

	2015	2014	2013
Bank of England	£0.5bn	£0.6bn	£0.6bn
US Federal Reserve	—	$1.3bn	$1.2bn
De Nederlandsche Bank	€0.2bn	€0.1bn	€0.1bn

35 Segmental analysis

(a) Reportable segments

The directors manage the Group primarily by class of business and present the segmental analysis on that basis. This includes the review of net interest income for each class of business - interest receivable and payable for all reportable segments is therefore presented net. Segments charge market prices for services rendered between each other; funding charges between segments are determined by RBS Treasury, having regard to commercial demands. The segment performance measure is operating profit/(loss).

Organisational structure

The Group continues to deliver on its plan to build a strong, simple and fair bank for both customers and shareholders. To support this and reflect the progress made on the initiatives above the previously reported operating segments have been realigned as follows:

Personal & Business Banking (PBB) comprises two reportable segments, UK Personal & Business Banking (UK PBB) and Ulster Bank RoI. UK PBB serves individuals and mass affluent customers in the UK together with small businesses (generally up to £2 million turnover). UK PBB includes Ulster Bank customers in Northern Ireland. Ulster Bank RoI serves individuals and businesses in the Republic of Ireland (RoI).

Commercial & Private Banking (CPB) comprises three reportable segments, Commercial Banking, Private Banking and RBS International (RBSI). Commercial Banking serves commercial and mid-corporate customers in the UK. Private Banking serves high net worth individuals in the UK and RBSI serves retail, commercial, corporate and financial institution customers in Jersey, Guernsey, Isle of Man and Gibraltar.

Corporate & Institutional Banking (CIB) serves UK and Western European corporate customers, and global financial institutions, supported by trading and distribution platforms in the UK, US and Singapore.

Capital Resolution consists of established businesses: CIB Capital Resolution and RBS Capital Resolution (RCR).

CIB Capital Resolution was created from non-strategic portfolios from CIB, to enable the build of a strong go-forward CIB business, consisting of three regional businesses (Americas, EMEA and APAC), Shipping, Markets assets, Other legacy assets including Global Transaction Services. There is a three stage process in place to guide the business down; starting with taking capital out, then running down the cost base and finally managing tail risk in the longer-term.

RCR was created on 1 January 2014 to de-risk the balance sheet. The original RBS Group perimeter was £47 billion of funded assets consisting of four asset groups: Ulster Bank (Ulster RCR), Real Estate Finance (ex. Ireland), Corporate and Markets. The remaining funded assets of £4.6 billion are included in Capital Resolution.

Williams & Glyn (W&G) comprises the RBS England and Wales branch-based businesses, along with certain SME and corporate activities across the UK. During the period presented W&G has not operated as a separate legal entity. The perimeter of the segment currently reported does not include certain portfolios that are ultimately intended to be divested as part of W&G, for example, certain NatWest branches in Scotland.

Central items & other comprises corporate functions, such as Treasury, Finance, Risk Management, Compliance, Legal, Communications and Human Resources. Central functions manages the Group capital resources and Group-wide regulatory projects and provides services to the reportable segments. Balances relating to Citizens and the international private banking business are also included.

Non-Core Division, established in 2009 as a principal vehicle for risk reduction, was dissolved on 31 December 2013.

Reporting changes

In line with the Group's strategy to be a simpler bank, the following reporting changes have been implemented in relation to the presentation of the Group results:

The following items previously reported separately after operating profit are now being reported within operating profit.

- Own credit adjustments;
- Gain/(loss) on redemption of own debt;
- Write-down of goodwill; and
- Strategic disposals.

Citizens Financial Group

Citizens was classified as a discontinued operation and as a disposal group on 31 December 2014 and its assets and liabilities from that date to 3 August 2015 have been aggregated and presented as separate lines in accordance with IFRS 5. On 3 August 2015, the Group's interest in Citizens fell to 20.9% and it was treated as an associate held for sale thereafter. On 30 October 2015, the Group sold its remaining shareholding in Citizens. Citizens is no longer treated as a reportable segment.

Comparatives have been restated accordingly for the changes outlined above.

35 Segmental analysis

2015	Net interest income £m	Non-interest income £m	Total income £m	Operating expenses £m	Depreciation and amortisation £m	Impairment recoveries/ (losses) £m	Operating profit/(loss) £m
UK Personal & Business Banking	4,263	998	5,261	(3,640)	—	7	1,628
Ulster Bank RoI	365	185	550	(383)	—	141	308
Personal & Business Banking	4,628	1,183	5,811	(4,023)	—	148	1,936
Commercial Banking	2,195	1,257	3,452	(1,395)	(141)	(69)	1,847
Private Banking	410	208	618	(1,018)	—	(13)	(413)
RBS International	303	64	367	(120)	—	—	247
Commercial & Private Banking	2,908	1,529	4,437	(2,533)	(141)	(82)	1,681
Corporate & Institutional Banking	82	1,440	1,522	(2,031)	—	5	(504)
Capital Resolution	440	(94)	346	(4,524)	(29)	781	(3,426)
Williams & Glyn	658	175	833	(387)	—	(15)	431
Central items & other	(308)	(490)	(798)	(1,470)	(1,003)	—	(3,271)
Total	8,408	3,743	12,151	(14,968)	(1,173)	837	(3,153)
2014*							
UK Personal & Business Banking	4,277	1,172	5,449	(3,632)	—	(154)	1,663
Ulster Bank RoI	467	137	604	(368)	—	306	542
Personal & Business Banking	4,744	1,309	6,053	(4,000)	—	152	2,205
Commercial Banking	2,130	1,331	3,461	(1,466)	(141)	(85)	1,769
Private Banking	454	235	689	(506)	—	5	188
RBS International	323	68	391	(117)	—	7	281
Commercial & Private Banking	2,907	1,634	4,541	(2,089)	(141)	(73)	2,238
Corporate & Institutional Banking	117	1,942	2,059	(2,259)	—	7	(193)
Capital Resolution	908	1,089	1,997	(1,796)	(28)	1,293	1,466
Williams & Glyn	664	188	852	(330)	—	(55)	467
Central items & other	(474)	(410)	(884)	(2,152)	(757)	13	(3,780)
Total	8,866	5,752	14,618	(12,626)	(926)	1,337	2,403

*Restated - refer to pages 148 and 248 for further details. Represented to reflect the segmental reorganisation.

35 Segmental analysis

2013*	Net interest income £m	Non-interest income £m	Total income £m	Operating expenses £m	Depreciation and amortisation £m	Impairment (losses)/ recoveries £m	Operating profit/(loss) £m
UK Personal & Business Banking	4,096	1,117	5,213	(3,995)	—	(669)	549
Ulster Bank RoI	478	428	906	(374)	—	(1,525)	(993)
Personal & Business Banking	4,574	1,545	6,119	(4,369)	—	(2,194)	(444)
Commercial Banking	2,021	1,379	3,400	(1,670)	(135)	(602)	993
Private Banking	419	240	659	(594)	—	(7)	58
RBS International	299	66	365	(128)	—	(47)	190
Commercial & Private Banking	2,739	1,685	4,424	(2,392)	(135)	(656)	1,241
Corporate & Institutional Banking	202	2,264	2,466	(1,809)	(118)	38	577
Capital Resolution	558	1,510	2,068	(4,293)	99	(663)	(2,789)
Williams & Glyn	657	199	856	(307)	—	(80)	469
Central items & other	(529)	714	185	(1,340)	(879)	(84)	(2,118)
Non-Core	429	208	637	(366)	(76)	(4,498)	(4,303)
Total	8,630	8,125	16,755	(14,876)	(1,109)	(8,137)	(7,367)

	2015			2014*			2013*		
Total revenue	External £m	Inter segment £m	Total £m	External £m	Inter segment £m	Total £m	External £m	Inter segment £m	Total £m
UK Personal & Business Banking	6,195	50	6,245	6,351	39	6,390	6,372	26	6,398
Ulster Bank RoI	640	15	655	672	50	722	1,057	58	1,115
Personal & Business Banking	6,835	65	6,900	7,023	89	7,112	7,429	84	7,513
Commercial Banking	3,482	42	3,524	3,554	51	3,605	3,640	31	3,671
Private Banking	577	191	768	624	240	864	651	298	949
RBS International	275	177	452	287	208	495	261	238	499
Commercial & Private Banking	4,334	410	4,744	4,465	499	4,964	4,552	567	5,119
Corporate & Institutional Banking	1,872	1,199	3,071	2,541	1,212	3,753	2,977	1,867	4,844
Capital Resolution	746	1,455	2,201	2,597	2,611	5,208	2,723	2,619	5,342
Williams & Glyn	920	—	920	954	—	954	988	—	988
Central items & other	1,587	(3,129)	(1,542)	1,819	(4,411)	(2,592)	3,382	(5,521)	(2,139)
Non-Core	n/a	n/a	n/a	n/a	n/a	n/a	1,117	384	1,501
Total	16,294	—	16,294	19,399	—	19,399	23,168	—	23,168

*Restated - refer to pages 148 and 248 for further details. Re-presented to reflect the segmental reorganisation.

35 Segmental analysis

Total income	2015 External £m	2015 Inter segment £m	2015 Total £m	2014* External £m	2014* Inter segment £m	2014* Total £m	2013* External £m	2013* Inter segment £m	2013* Total £m
UK Personal & Business Banking	5,199	62	5,261	5,351	98	5,449	5,074	139	5,213
Ulster Bank RoI	569	(19)	550	559	45	604	935	(29)	906
Personal & Business Banking	5,768	43	5,811	5,910	143	6,053	6,009	110	6,119
Commercial Banking	3,817	(365)	3,452	3,806	(345)	3,461	3,756	(356)	3,400
Private Banking	508	110	618	542	147	689	459	200	659
RBS International	200	167	367	195	196	391	141	224	365
Commercial & Private Banking	4,525	(88)	4,437	4,543	(2)	4,541	4,356	68	4,424
Corporate & Institutional Banking	1,557	(35)	1,522	2,178	(119)	2,059	2,452	14	2,466
Capital Resolution	446	(100)	346	2,036	(39)	1,997	1,849	219	2,068
Williams & Glyn	852	(19)	833	872	(20)	852	871	(15)	856
Central items & other	(997)	199	(798)	(921)	37	(884)	247	(62)	185
Non-Core	n/a	n/a	n/a	n/a	n/a	n/a	971	(334)	637
Total	12,151	—	12,151	14,618	—	14,618	16,755	—	16,755

	2015 Assets £m	2015 Liabilities £m	2015 Cost to acquire fixed assets and intangible assets £m	2014* Assets £m	2014* Liabilities £m	2014* Cost to acquire fixed assets and intangible assets £m	2013* Assets £m	2013* Liabilities £m	2013* Cost to acquire fixed assets and intangible assets £m
UK Personal & Business Banking	127,067	140,585	—	119,763	136,823	—	117,368	131,744	5
Ulster Bank RoI	21,264	15,837	—	22,479	17,962	—	22,954	19,976	6
Personal & Business Banking	148,331	156,422	—	142,242	154,785	—	140,322	151,720	11
Commercial Banking	96,983	94,849	214	90,677	89,772	218	89,706	96,065	83
Private Banking	11,596	23,256	—	12,241	22,660	21	12,299	22,537	27
RBS International	7,854	21,399	—	7,779	20,995	—	6,923	21,059	—
Commercial & Private Banking	116,433	139,504	214	110,697	133,427	239	108,928	139,661	110
Corporate & Institutional Banking	213,790	194,238	10	281,910	261,472	—	247,972	223,964	—
Capital Resolution	187,833	186,458	3	314,449	277,858	135	305,415	274,808	437
Williams & Glyn	20,117	24,171	—	19,563	22,065	—	19,836	21,579	—
Central items & other	125,687	69,491	1,221	176,521	148,087	1,041	170,475	154,596	1,096
Non-Core	n/a	n/a	n/a	n/a	n/a	n/a	26,930	4,769	18
Total	812,191	770,284	1,448	1,045,382	997,694	1,415	1,019,878	971,097	1,672

*Restated - refer to pages 148 and 248 for further details. Re-presented to reflect the segmental reorganisation.

35 Segmental analysis

Segmental analysis of assets and liabilities included in disposal groups:

	2015		2014*		2013*	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Commercial Banking	—	—	2	—	—	—
Private Banking	—	—	—	—	3	—
Commercial & Private Banking	—	—	2	—	3	—
Corporate & Institutional Banking	—	—	18	14	—	—
Capital Resolution	130	251	46	2	—	—
Central items & other	3,356	2,729	80,967	71,268	680	3,190
Non-Core	n/a	n/a	n/a	n/a	107	20
Total	3,486	2,980	81,033	71,284	790	3,210

Segmental analysis of goodwill is as follows:

	UK Personal & Business Banking £m	Commercial Banking £m	Private Banking £m	RBSI £m	Capital Resolution £m	Central items (1) £m	Total £m
At 1 January 2014*	3,342	1,907	715	300	130	3,736	10,130
Transfer to disposal groups	—	—	—	—	—	(3,957)	(3,957)
Currency translation and other adjustments	—	—	(9)	—	—	221	212
Write down of goodwill - continuing operations	—	—	—	—	(130)	—	(130)
At 1 January 2015*	3,342	1,907	706	300	—	—	6,255
Transfer to disposal groups	—	—	(220)	—	—	—	(220)
Currency translation and other adjustments	—	—	12	—	—	—	12
Write down of goodwill - continuing operations	—	—	(498)	—	—	—	(498)
At 31 December 2015	3,342	1,907	—	300	—	—	5,549

*Restated - refer to pages 148 and 248 for further details. Re-presented to reflect the segmental reorganisation.

Note:

(1) Relates to Citizens Financial Group

35 Segmental analysis

(b) Geographical segments

The geographical analysis in the tables below has been compiled on the basis of location of office where the transactions are recorded.

2015	UK £m	USA £m	Europe £m	Rest of the World £m	Total £m
Total revenue	14,494	346	1,202	252	16,294
Net interest income	7,516	144	602	146	8,408
Net fees and commissions	2,340	138	338	71	2,887
Income from trading activities	819	44	115	(24)	954
Other operating income	41	(68)	(34)	(37)	(98)
Total income	10,716	258	1,021	156	12,151
Operating (loss)/profit before tax	(662)	(2,622)	449	(318)	(3,153)
Total assets	677,248	77,955	38,258	18,730	812,191
Of which assets held for sale	—	15	1,251	2,220	3,486
Total liabilities	644,067	76,618	31,268	18,331	770,284
Of which liabilities held for sale	—	16	418	2,546	2,980
Net assets attributable to equity shareholders and non-controlling interests	33,181	1,337	6,990	399	41,907
Contingent liabilities and commitments	128,478	9,729	11,148	692	150,047
Cost to acquire property, plant and equipment and intangible assets	1,330	70	21	27	1,448
2014*					
Total revenue	15,750	1,236	1,869	544	19,399
Net interest income	7,587	217	793	269	8,866
Net fees and commissions	2,548	285	497	148	3,478
Income from trading activities	350	547	265	28	1,190
Other operating income	958	71	75	(20)	1,084
Total income	11,443	1,120	1,630	425	14,618
Operating profit/(loss) before tax	441	382	1,626	(46)	2,403
Total assets	783,430	183,174	45,961	32,817	1,045,382
Of which assets held for sale	48	80,985	—	—	81,033
Total liabilities	757,650	167,421	40,454	32,169	997,694
Of which liabilities held for sale	2	71,282	—	—	71,284
Net assets attributable to equity shareholders and non-controlling interests	25,780	15,753	5,507	648	47,688
Contingent liabilities and commitments	104,369	88,967	37,273	4,258	234,867
Cost to acquire property, plant and equipment and intangible assets	1,025	238	133	19	1,415
2013*					
Total revenue	16,541	2,099	3,208	1,320	23,168
Net interest income	7,531	248	790	61	8,630
Net fees and commissions	2,484	325	729	168	3,706
Income from trading activities	1,583	885	199	193	2,860
Other operating income	792	162	605	—	1,559
Total income	12,390	1,620	2,323	422	16,755
Operating loss before tax	(2,356)	(1,187)	(3,706)	(118)	(7,367)
Total assets	731,304	199,305	51,763	37,506	1,019,878
Of which assets held for sale	—	750	38	2	790
Total liabilities	703,739	184,286	46,139	36,933	971,097
Of which liabilities held for sale	—	3,210	—	—	3,210
Net assets attributable to equity shareholders and non-controlling interests	27,565	15,019	5,624	573	48,781
Contingent liabilities and commitments	108,274	82,758	40,961	5,095	237,088
Cost to acquire property, plant and equipment and intangible assets	1,035	412	217	8	1,672

*Restated - refer to pages 148 for further details.

36 Directors' and key management remuneration

The directors of the Bank are also directors of the holding company and are remunerated for their services to the RBS Group as a whole. The remuneration of the directors is disclosed in the Report and Accounts of the RBS Group.

Compensation of key management

The aggregate remuneration of directors and other members of key management during the year, borne by the RBS Group, was as follows:

	2015 £000	2014 £000
Short-term benefits	19,395	20,917
Post-employment benefits	435	1,964
Termination benefits	—	3,481
Share-based payments	3,472	4,889
	23,302	31,251

Key management comprises members of the RBS Group Executive Committee.

37 Transactions with directors and key management

(a) At 31 December 2015, amounts outstanding in relation to transactions, arrangements and agreements entered into by authorised institutions in the Group, as defined in UK legislation, were £129,070 in respect of loans to four persons who were directors of the company at any time during the financial period.

(b) For the purposes of IAS 24 'Related Party Disclosures', key management comprise directors of the Bank and members of the RBS Group Executive Committee. The captions in the Group's primary financial statements include the following amounts attributable, in aggregate, to key management:

	2015 £000	2014 £000
Loans and advances to customers	2,741	4,089
Customer accounts	12,332	22,037

Key management have banking relationships with Group entities which are entered into in the normal course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with other persons of a similar standing or, where applicable, with other employees. These transactions did not involve more than the normal risk of repayment or present other unfavourable features.

Key management had no reportable transactions or balances with the holding company.

38 Related parties

UK Government

On 1 December 2008, the UK Government through HM Treasury became the ultimate controlling party of The Royal Bank of Scotland Group plc. The UK Government's shareholding is managed by UK Financial Investments Limited, a company wholly owned by the UK Government. As a result, the UK Government and UK Government controlled bodies became related parties of the Group. During 2015, all of the B shares held by the UK Government were converted into ordinary shares of £1 each and the Dividend Access Share Retirement Agreement was agreed between RBS plc and HM Treasury.

The Group enters into transactions with many of these bodies on an arm's length basis. Transactions include the payment of: taxes principally UK corporation tax (page 175) and value added tax; national insurance contributions; local authority rates; and regulatory fees and levies (including the bank levy and FSCS levies (page 233); together with banking transactions such as loans and deposits undertaken in the normal course of banker-customer relationships.

Bank of England facilities

The Group may participates in a number of schemes operated by the Bank of England in the normal course of business.

Members of the Group that are UK authorised institutions are required to maintain non-interest bearing (cash ratio) deposits with the Bank of England amounting to 0.18% of their average eligible liabilities in excess of £600 million. They also have access to Bank of England reserve accounts: sterling current accounts that earn interest at the Bank of England Rate.

The table below discloses items included in income and operating expenses on transactions between the Group and fellow subsidiaries of the RBS Group.

Other related parties

(a) In their roles as providers of finance, Group companies provide development and other types of capital support to businesses. These investments are made in the normal course of business and on arm's length terms. In some instances, the investment may extend to ownership or control over 20% or more of the voting rights of the investee company. However, these investments are not considered to give rise to transactions of a materiality requiring disclosure under IAS 24.

(b) The Group recharges The Royal Bank of Scotland Group Pension Fund with the cost of administration services incurred by it. The amounts involved are not material to the Group.

(c) In accordance with IAS 24, transactions or balances between Group entities that have been eliminated on consolidation are not reported.

(d) The captions in the primary financial statements of the parent company include amounts attributable to subsidiaries. These amounts have been disclosed in aggregate in the relevant notes to the financial statements.

The table below discloses items included in income and operating expenses on transactions between the Group and fellow subsidiaries of the RBS Group.

	2015 £m	2014 £m	2013 £m
Income			
Interest receivable	90	87	158
Interest payable	1,019	1,032	1,020
Fees and commissions receivable	7	7	13
Fees and commissions payable	2	3	79
Net (expense)/income from discontinued operations	(28)	(28)	6

39 Ultimate holding company

The Group's ultimate holding company is The Royal Bank of Scotland Group plc which is incorporated in Great Britain and registered in Scotland. As at 31 December 2015, The Royal Bank of Scotland Group plc heads the largest group in which the Group is consolidated. Copies of the consolidated accounts may be obtained from The Secretary, The Royal Bank of Scotland Group plc, Gogarburn, PO Box 1000, Edinburgh EH12 1HQ.

Following placing and open offers by The Royal Bank of Scotland Group plc in December 2008 and April 2009, the UK Government, through HM Treasury, currently holds 72.6% of the issued ordinary share capital of the holding company and is therefore the Group's ultimate controlling party.

40 Post balance sheet events

Pension fund

Subsequently and pursuant to the Memorandum of Understanding, the RBS Group agreed with the Trustee a Statement of Funding Principles in relation to an actuarial valuation as at 31 December 2015. The RBS Group and Trustee also updated the existing Schedule of Contributions and Recovery Plan to reflect the £4.2 billion contribution, which was paid during March 2016.

41 Related undertakings

Group legal entities and activities at 31 December 2015

In accordance with the Companies Act 2006, the company's related undertakings and the accounting treatment for each are listed below. All undertakings are wholly-owned by the company or subsidiaries of the company and are consolidated by reason of contractual control (Section 1162(2) CA 2006), unless otherwise indicated. Group interest refers to ordinary shares of equal values and voting rights unless further analysis is provided in the footnotes. Activities are classified in accordance with Annex I to the Capital Requirements Directive ("CRD IV") and the definitions in Article 4 of the Capital Requirements Regulation.

The following table details active related undertakings incorporated in the United Kingdom which are 100% owned by the Group and fully consolidated for accounting purposes.

Enitity name	Activity(1)
Adam & Company Group PLC	BF
Adam & Company Investment Management Ltd	BF
Adam & Company PLC	CI
Caledonian Sleepers Rail Leasing Ltd	BF
Care Homes 1 Ltd	OTH
Care Homes 2 Ltd	OTH
Care Homes 3 Ltd	OTH
Care Homes Holdings Ltd	OTH
Churchill Management Ltd	OTH
Coutts & Company	CI
Coutts Finance Company	BF
Desertlands Entertainment Ltd	BF
Distant Planet Productions Ltd	BF
Dixon Motors Developments Ltd	BF
Euro Sales Finance Plc	BF
Farming and Agricultural Finance Ltd	BF
G L Trains Ltd	BF
Gatehouse Way Developments Ltd	OTH
GRG Real Estate Asset Management (Great Britain) Ltd	BF
Heartlands (Central) Ltd	OTH
Helena Productions Ltd	BF
KUC (Public Houses) Ltd	OTH
KUC Holdings Ltd	OTH
KUC Properties Ltd	OTH
Land Options (West) Ltd	OTH
Latam Directors Ltd	BF
Leckhampton Finance Ltd	BF
Libra No 1 Ltd	OTH
Lombard & Ulster Ltd	BF
Lombard Asset Leasing Ltd	BF
Lombard Business Finance Ltd	BF
Lombard Business Leasing Ltd	BF
Lombard Charterhire Ltd	BF
Lombard Corporate Finance (3) Ltd	BF
Lombard Corporate Finance (6) Ltd	BF
Lombard Corporate Finance (7) Ltd	BF
Lombard Corporate Finance (10) Ltd	BF
Lombard Corporate Finance (11) Ltd	BF
Lombard Corporate Finance (13) Ltd	BF
Lombard Corporate Finance (14) Ltd	BF
Lombard Corporate Finance (15) Ltd	BF
Lombard Corporate Finance (December 1) Ltd	BF
Lombard Corporate Finance (December 3) Ltd	BF
Lombard Corporate Finance (June 2) Ltd	BF
Lombard Corporate Finance (March 1) Ltd	BF
Lombard Discount Ltd	BF
Lombard Facilities Ltd	BF
Lombard Finance Ltd	BF
Lombard Initial Leasing Ltd	BF
Lombard Leasing Contracts Ltd	BF
Lombard Lessors Ltd	BF
Lombard Maritime Ltd	BF
Lombard North Central Leasing Ltd	BF

Enitity name	Activity(1)
Lombard North Central PLC	BF
Lombard Property Facilities Ltd	BF
Lombard Technology Services Ltd	BF
Lombard Vehicle Management (1) Ltd	BF
Lombard Vehicle Management (2) Ltd	BF
Lombard Vehicle Management (3) Ltd	BF
Lombard Vehicle Management Ltd	BF
Lombard Venture Finance Ltd	BF
Nanny McPhee Productions Ltd	BF
National Westminster Bank Plc	CI
National Westminster Home Loans Ltd	BF
National Westminster Properties No. 1 Ltd	SC
NatWest (HMHP) Ltd	BF
NatWest Capital Finance Ltd	BF
NatWest Corporate Investments	BF
NatWest Finance Ltd	OTH
NatWest Leasing and Asset Finance Ltd	BF
NatWest Machinery Leasing Ltd	BF
NatWest Property Investments Ltd	OTH
NatWest Specialised Property Investments Ltd	BF
NatWest Ventures Investments Ltd	BF
Nevis Derivatives No. 3 LLP	BF
Nevis Derivatives No. 2 LLP	BF
Nevis Derivatives No.1 LLP	BF
Northants Developments Ltd	BF
Northern Isles Ferries Ltd	BF
P of A Productions Ltd	BF
Patalex II Productions Ltd	BF
Patalex III Productions Ltd	BF
Patalex IV Productions Ltd	BF
Patalex Productions Ltd	BF
Patalex V Productions Ltd	BF
Pittville Leasing Ltd	BF
Premier Audit Company Ltd	BF
Price Productions Ltd	BF
Primemodern Ltd	OTH
Priority Sites Investments Ltd	BF
Priority Sites Ltd	OTH
Property Venture Partners Ltd	OTH
Property Ventures (B&M) Ltd	OTH
R.B. Asset Value Ltd	BF
R.B. Capital Leasing Ltd	BF
R.B. Equipment Leasing Ltd	BF
R.B. Investment Holdings Ltd	BF
R.B. Leasing (April) Ltd	BF
R.B. Leasing (Bluewater) Ltd	BF
R.B. Leasing (December) Ltd	BF
R.B. Leasing (Eden) Ltd	BF
R.B. Leasing (March) Ltd	BF
R.B. Leasing (September) Ltd	BF
R.B. Leasing Company Ltd	BF

For notes to this table refer to page 264.

41 Related undertakings continued

Enitity name	Activity(1)
R.B. Quadrangle Leasing Ltd	BF
R.B.S. Special Investments Ltd	BF
RB Investments 2 Ltd	BF
RB Investments 3 Ltd	OTH
RBDC Administrator Ltd	OTH
RBDC Investments Ltd	OTH
RBEF Ltd	OTH
RBS Argonaut Ltd	OTH
RBS Asset Finance Europe Ltd	BF
RBS Asset Management (ACD) Ltd	BF
RBS Asset Management Holdings	BF
RBS Asset Management Ltd	BF
RBS Hotel Development Company Ltd	OTH
RBS Hotel Investments Ltd	OTH
RBS Investment Ltd	BF
RBS Invoice Finance Ltd	BF
RBS Mezzanine Ltd	BF
RBS Property Developments Ltd	OTH
RBS Property Ventures Investments Ltd	BF
RBS Residential Venture No.1 Ltd	OTH
RBS Secured Funding LLP	BF
RBS SME Investments Ltd	OTH
RBS Special Opportunities General Partner (England) Ltd	BF
RBS Special Opportunities General Partner (Scotland) II Ltd	BF
RBS Special Opportunities General Partner (Scotland) Ltd	OTH
RBS Specialised Property Investments Ltd	OTH
RBSG (Europe)	BF
RBSG International Holdings Ltd	BF
RBSM (Investments) Ltd	CI
RBSM Capital Ltd	BF
RBSSAF (2) Ltd	BF
RBSSAF (3) Ltd	BF
RBSSAF (4) Ltd	BF
RBSSAF (6) Ltd	BF
RBSSAF (7) Ltd	BF
RBSSAF (8) Ltd	BF
RBSSAF (10) Ltd	BF

For notes to this table refer to page 264.

Enitity name	Activity(1)
RBSSAF (11) Ltd	BF
RBSSAF (12) Ltd	BF
RBSSAF (13) Ltd	BF
RBSSAF (16) Ltd	BF
RBSSAF (19) Ltd	BF
RBSSAF (22) Ltd	BF
RBSSAF (23) Ltd	BF
RBSSAF (25) Ltd	BF
RBSSAF (26) Ltd	BF
Riossi Ltd	BF
RoboScot DevCap Ltd	OTH
RoboScot Equity Ltd	OTH
RoboScot Ventures Ltd	OTH
Royal Bank Asset Finance Ltd	BF
Royal Bank Development Capital Ltd	BF
Royal Bank Investments Ltd	BF
Royal Bank Invoice Finance Ltd	BF
Royal Bank Leasing Ltd	BF
Royal Bank of Scotland (Industrial Leasing) Ltd	BF
Royal Bank Operating Leasing Ltd	BF
Royal Bank Project Investments Ltd	OTH
Royal Bank Ventures Investments Ltd	BF
Royal Bank Ventures Ltd	BF
Royal Scot Leasing Ltd	BF
RoyScot Financial Services Ltd	BF
RoyScot Larch Ltd	BF
RoyScot Trust plc	BF
Sandford Leasing Ltd	BF
SIG 1 Holdings Ltd	BF
SIG Number 2 Ltd	OTH
Springwell Street Developments (No 1) Ltd	OTH
STAR 1 Special Partner Ltd	BF
Style Financial Services Ltd	BF
The One Account Ltd	BF
The Royal Bank of Scotland Invoice Discounting Ltd	BF
Theobald Film Productions LLP	BF
Thrapston Triangle Ltd	OTH
Total Capital Finance Ltd	BF
UB SIG (NI) Ltd	BF
Ulster Bank Commercial Services (NI) Ltd	BF
Ulster Bank Ltd	CI
Ulster Bank Pension Trustees Ltd	OTH
Voyager Leasing Ltd	BF
W. & G. Industrial Leasing Ltd	BF
W. & G. Lease Finance Ltd	BF
Walton Lake Developments Ltd	OTH
West Register (Bankside) Ltd	OTH
West Register (Hotels Number 1) Ltd	OTH
West Register (Hotels Number 2) Ltd	OTH
West Register (Hotels Number 3) Ltd	OTH
West Register (Land) Ltd	OTH
West Register (Northern Ireland) Property Ltd	BF
West Register (Project Developments) Ltd	BF
West Register (Property Investments) Ltd	BF
West Register (Realisations) Ltd	OTH
West Register (Residential Property Investments) Ltd	OTH
West Register Hotels (Holdings) Ltd	BF
Williams & Glyn's Leasing Company Ltd	OTH
Winchcombe Finance Ltd	BF
WR (NI) Property Investments Ltd	BF
WR (NI) Property Realisations Ltd	OTH

The following table details active related undertakings incorporated outside the United Kingdom which are 100% owned by the Group and fully consolidated for accounting purposes.

Country	Enitity name	Activity(1)
Australia	RBS (Australia) Pty Ltd	BF
Bermuda	R.B. Leasing BDA One Ltd	BF
Brazil	RBS Assessoria Ltda	SC
Cayman Islands	Coutts & Co (Cayman) Ltd	CI
Cayman Islands	Coutts General Partner (Cayman) V Ltd	OTH
Cayman Islands	Equator Investments (Cayman) Ltd	BF
Cayman Islands	Islay Investments Ltd	OTH
Cayman Islands	NatWest (Deansgate) Investments Ltd	OTH
Cayman Islands	RBS Special Opportunities General Partner (Cayman) Ltd	OTH
Cayman Islands	Redlion Investments Ltd	OTH
Cayman Islands	Ringwold Investments Ltd	OTH
Cayman Islands	Royhaven Secretaries Ltd	BF
Finland	Artul Kiinteistöt Oy	BF
Finland	Fab Ekenäs Formanshagen 4	SC
Finland	Forssa Liikekiinteistöt Oy	BF
Finland	Koy Espoon Entresse II	BF
Finland	Koy Espoon Niittysillantie 5	BF
Finland	Koy Helsingin Mechelininkatu 1	BF
Finland	Koy Helsingin Osmontie 34	BF
Finland	Koy Helsingin Panuntie 11	BF
Finland	Koy Helsingin Panuntie 6	BF
Finland	Koy Iisalmen Kihlavirta	BF
Finland	Koy Jämsän Keskushovi	BF
Finland	Koy Kokkolan Kaarlenportti Fab	BF
Finland	Koy Kouvolan Oikeus ja Poliisitalo	BF
Finland	Koy Lohjan Huonekalutalo	BF
Finland	Koy Millennium	BF
Finland	Koy Nummelan Portti	BF
Finland	Koy Nuolialan päiväkoti	BF
Finland	Koy Otapuisto	BF
Finland	Koy Päiväläisentie 1-6	BF
Finland	Koy Raision Kihlakulma	BF
Finland	Koy Ravattulan Kauppakeskus	BF
Finland	Koy Tapiolan Louhi	BF
Finland	Koy Vapaalan Service-Center	BF
Finland	Nordisk Renting Oy	BF
France	RBS France Holdings SARL	BF
France	RDS Metropolis SAS	BF
Germany	patus 455. GmbH	BF
Germany	RBS (Deutschland) AG	CI
Germany	RBS Deutschland Holdings GmbH	BF

For notes for this table refer to page 264.

Country	Enitity name	Activity(1)
Germany	RBS Real Estate Holdings Germany GmbH	SC
Germany	RBS Structured Financial Services GmbH	BF
Germany	West Register PRIME Düsseldorf 2 GmbH	BF
Germany	West Register PRIME Holding GmbH	OTH
Gibraltar	Gosport Ltd	OTH
Gibraltar	RBS (Gibraltar) Ltd	CI
Gibraltar	Sotomar Ltd	BF
Guernsey	Drummonds Insurance PCC Ltd	BF
Guernsey	Lothbury Insurance Company Ltd	BF
Guernsey	Morar ICC Insurance Ltd	BF
Guernsey	RBS Employment (Guernsey) Ltd	SC
Guernsey	RoyScot Guernsey Ltd	BF
Hong Kong	RBS Securities Japan Ltd	BF
India	RBS Business Services Private Ltd	OTH
India	RBS India Development Centre Private Ltd	OTH
Republic of Ireland	Easycash (Ireland) Ltd	BF
Republic of Ireland	First Active Holdings Ltd	BF
Republic of Ireland	First Active Insurances Services Ltd	BF
Republic of Ireland	First Active Investments No. 4 Ltd	BF
Republic of Ireland	First Active Treasury plc	BF
Republic of Ireland	Hume Street Nominees Ltd	OTH
Republic of Ireland	Lombard Ireland Group Holdings	BF
Republic of Ireland	Lombard Ireland Ltd	BF
Republic of Ireland	National Westminster Services (Ireland) Ltd	SC
Republic of Ireland	Norgay Property Ltd	BF
Republic of Ireland	RBS Asset Management (Dublin) Ltd	BF
Republic of Ireland	The RBS Group Ireland Retirement Savings Trustee Ltd	OTH
Republic of Ireland	UB SIG (ROI) Ltd	BF
Republic of Ireland	Ulster Bank (Ireland) Holdings	BF
Republic of Ireland	Ulster Bank Commercial Services Ltd	BF
Republic of Ireland	Ulster Bank Dublin Trust Company	BF
Republic of Ireland	Ulster Bank Holdings (ROI) Ltd	BF
Republic of Ireland	Ulster Bank Ireland Ltd	CI
Republic of Ireland	Ulster Bank Pension Trustees (RI) Ltd	OTH
Republic of Ireland	Ulster Bank Wealth	BF

41 Related undertakings continued

Country	Enitity name	Activity(1)
Republic of Ireland	Walter Property Ltd	BF
Republic of Ireland	West Register (Republic of Ireland) Property Ltd	BF
Isle Of Man	Coutts & Co (Manx) Ltd	BF
Isle Of Man	Isle of Man Bank (Nominees) Ltd	BF
Isle Of Man	Isle of Man Bank Ltd	CI
Isle Of Man	Lombard Manx Leasing Ltd	BF
Isle Of Man	Lombard Manx Ltd	BF
Isle Of Man	The Royal Bank of Scotland Employment (Isle of Man) Ltd	BF
Jersey	C.J. Fiduciaries Ltd	BF
Jersey	Citron 2004 Ltd	BF
Jersey	Coutts & Co Trustees (Jersey) Ltd	BF
Jersey	Fidelis Nominees Ltd	BF
Jersey	Lombard Finance (CI) Ltd	BF
Jersey	Magnus Nominees Ltd	BF
Jersey	Mulcaster Street Nominees Ltd	OTH
Jersey	Pitstop Ltd	OTH
Jersey	RBS International Employees' Pension Trustees Ltd	BF
Jersey	Rostand Nominees Ltd	BF
Jersey	Rouge 2004 Ltd	BF
Jersey	RoyScot Jersey Ltd	BF
Jersey	The Royal Bank of Scotland International (Holdings) Ltd	BF
Jersey	The Royal Bank of Scotland International Ltd	CI
Jersey	Vert 2004 Ltd	OTH
Kazakhstan	JSC SB RBS (Kazakhstan)	BF
Netherlands	National Westminster International Holdings B.V.	BF
Netherlands	NatWest Securities B.V.	BF
Netherlands	RBS Investments Netherlands B.V.	BF
Netherlands	RBS Netherlands B.V.	BF
Netherlands	RBS Netherlands Holdings B.V.	BF
Netherlands	RBS-CBFM Netherlands B.V.	BF
Norway	BD Lagerhus AS	BF
Norway	Eiendomsselskapet Apteno Larvik AS	BF
Norway	Hatros 1 AS	BF
Norway	Nordisk Renting AS	BF

For notes for this table refer to page 264.

Country	Enitity name	Activity(1)
Norway	Ringdalveien 20 AS	BF
Panama	Growth Advisors S.A.	BF
Panama	Steering Group SA	BF
Poland	RBS Bank (Polska) S.A.	CI
Poland	RBS Polish Financial Advisory Services sp. z o.o.	OTH
Russia	The Royal Bank of Scotland ZAO	CI
Sweden	Arkivborgen KB	BF
Sweden	Backsmedjan KB	BF
Sweden	Bil Fastigheter i Sverige AB	BF
Sweden	Bilfastighet i Täby AB	BF
Sweden	Braheberget KB	BF
Sweden	Brödmagasinet KB	BF
Sweden	Dalklockan 6 KB	BF
Sweden	Eurohill 4 KB	BF
Sweden	Fastighet Kallebäck 2:4 i Göteborg AB	BF
Sweden	Fastighets AB Flöjten i Norrköping	BF
Sweden	Fastighets AB Hammarbyvagnen	BF
Sweden	Fastighets AB Kabisten 1	BF
Sweden	Fastighets AB Stockmakaren	BF
Sweden	Fastighets AB Xalam	BF
Sweden	Fastighets AB Sambiblioteket	BF
Sweden	Fastighetsbolaget Holma i Höör AB	BF
Sweden	Forskningshöjden KB	BF
Sweden	Förvaltningsbolaget Dalkyrkan KB	BF
Sweden	Förvaltningsbolaget Predio 3 KB	BF
Sweden	Gredelinen KB	BF
Sweden	Grinnhagen KB	BF
Sweden	Horrsta 4:38 KB	BF
Sweden	IR Fastighets AB	BF
Sweden	IR IndustriRenting AB	BF
Sweden	Kallebäck Institutfastigheter AB	BF
Sweden	KB Eurohill	BF
Sweden	KB IR Gamlestaden	BF
Sweden	KB Lagermannen	BF
Sweden	KB Likriktaren	BF
Sweden	Läkten 1 KB	BF
Sweden	LerumsKrysset KB	BF
Sweden	Limstagården KB	OTH
Sweden	Mjälgen KB	BF
Sweden	Nordisk Renting AB	BF
Sweden	Nordisk Renting HB	BF
Sweden	Nordisk Specialinvest AB	BF
Sweden	Nordiska Strategifastigheter Holding AB	BF
Sweden	Pyrrhula 6,7 AB	BF
Sweden	SFK Kommunfastigheter AB	BF
Sweden	Sjöklockan KB	BF
Sweden	Skinnarängen KB	BF
Sweden	Solbänken KB	BF
Sweden	Strand European Holdings AB	BF
Sweden	Svenskt Fastighetskapital AB	OTH
Sweden	Svenskt Fastighetskapital Holding AB	BF
Sweden	Tingsbrogården KB	BF
Sweden	Tygverkstaden 1 KB	BF
Sweden	Vansbro Fjärrvärme KB	BF
Sweden	Vansbroviken KB	BF
Switzerland	Coutts & Co Ltd	CI
Switzerland	Coutts & Co Trustees (Suisse) S.A.	OTH

41 Related undertakings continued

Country	Enitity name	Activity(1)
Switzerland	RBS Services (Switzerland) Ltd	OTH
United Arab Emirates	RBS Operations FZ LLC	SC
United States	Candlelight Acquisition LLC	OTH
United States	Communications Capital Group I, LLC	BF
United States	Communications Capital Group II, LLC	BF
United States	Financial Asset Securities Corp.	BF
United States	Gil Holdings LLC	BF
United States	Governor Acquisition Company, LLC	OTH
United States	Greenwich Capital Derivatives, Inc.	BF
United States	Harborview Commercial Holdings I, LLC	BF
United States	Kelts LLC	BF
United States	Lease Plan North America LLC	BF
United States	NatWest Group Holdings Corp	BF
United States	Random Properties Acquisition Corp. I	OTH
United States	Random Properties Acquisition Corp. II	OTH
United States	Random Properties Acquisition Corp. III	OTH

Country	Enitity name	Activity(1)
United States	Random Properties Acquisition Corp. IV	OTH
United States	RBS Acceptance Inc.	CI
United States	RBS Americas Property Corp.	SC
United States	RBS Commercial Funding Inc.	BF
United States	RBS Equity Corp	BF
United States	RBS Financial Products Inc.	BF
United States	RBS Holdings USA Inc.	BF
United States	RBS Investments USA Corp.	BF
United States	RBS Securities Inc.	BF
United States	RBS Smart Products Inc	BF
United States	Rimfort Corp	BF
United States	Surprise Acquisition Company, LLC	OTH
Virgin Islands, British	Action Corporate Services Ltd	BF
Virgin Islands, British	Fountainhead Consultants Ltd	BF
Virgin Islands, British	JMJ Holdings Ltd	BF

For notes for this table refer to page 264.

The following table details active related undertakings incorporated in the United Kingdom where the Group ownership is less than 100%.

Enitity name	Activity(1)	Accounting treatment(2)	Group interest %	Notes
Adam & Company General Partner Ltd	BF	IA	50	
Aspire Oil Services Ltd	BF	EAA	28	
Attraction Inns Ltd	BF	IA	30	
Ballymore (London Arena) Ltd	OTH	IA	45	
Business Growth Fund plc	BF	EAA	24	
Cala Campus Ltd	OTH	EAJV	50	
CFN Packaging Group Ltd	OTH	IA	25	
Cloud Electronics Holdings Ltd	BF	IA	20	
Coneworx Ltd	OTH	IA	40	
DF Ventures Ltd	BF	IA	20	
Entaco Group Ltd	BF	IA	33	
Ferrostatics Holdings Ltd	BF	IA	35	
Flats 4 U Ltd	OTH	IA	30	
Forest Garden Group Ltd	OTH	IA	28	
GATX Asset Residual Management Ltd	OTH	EAA	50	
GWNW City Developments Ltd	OTH	EAJV	50	
Higher Broughton (GP) Ltd	BF	EAA	41	
Isobel AssetCo Ltd	SC	FC	75	
Isobel EquityCo Ltd	BF	FC	75	
Isobel HoldCo Ltd	BF	FC	75	
Isobel Intermediate HoldCo Ltd	BF	FC	75	
Isobel Loan Capital Ltd	BF	FC	75	
Isobel Mezzanine Borrower Ltd	BF	FC	75	
Jaguar Cars Finance Ltd	BF	FC	50	
JCB Finance (Leasing) Ltd	BF	FC	75	
JCB Finance Ltd	BF	FC	75	
Kangaroo Holdings Ltd	BF	IA	42	(3)
Land Options (East) Ltd	BF	EAJV	50	
Lombard GATX Holdings Ltd	BF	EAJV	50	
MSW Ltd	OTH	IA	20	
Omega Warrington Ltd	OTH	EAJV	50	

Enitity name	Activity(1)	Accounting treatment(2)	Group interest %	Notes
Pad55 Pickering Commonhold Association Ltd	OTH	FC	94	
Pollokshields Developments Ltd	OTH	IA	49	
Prestige Walker Ltd	OTH	IA	30	
Race 500 Ltd	BF	IA	21	
RBS Covered Bonds (LM) Ltd	BF	IA	20	
RBS Covered Bonds LLP	BF	FC	99	
RBS Secured Funding (LM) Ltd	BF	FC	20	(4)
RBS Sempra Commodities LLP	BF	FC	51	
RBS Sempra Products Ltd	OTH	FC	51	
Salwan Pharmacy Ltd	OTH	IA	20	
Star Capital Partners Investments LLP	BF	IA	40	
Sutherland Trading Company Ltd	OTH	IA	25	
Tay Valley Lighting (Leeds) Ltd	OTH	EAJV	50	
Tay Valley Lighting (Newcastle and North Tyneside) Ltd	OTH	EAJV	50	
Tay Valley Lighting (Stoke on Trent) Ltd	OTH	EAJV	50	
Telford Homes (Stratford) Ltd	OTH	EAJV	50	
The Appeal Group Ltd	OTH	IA	25	
The Scottish Agricultural Securities Corporation P.L.C.	BF	IA	33	
The Storage Pod Ltd	OTH	IA	48	
Topco (No1) Ltd	OTH	IA	45	
Uniconn Ltd	OTH	IA	30	
Vocalink Holdings Ltd	BF	EAA	21	
Wealdland Ltd	OTH	IA	29	
Welsh Industrial Partnership (GP) Ltd	BF	FC	51	
Yorkmarsh Ltd	BF	IA	30	

For notes to this table refer to page 264.

The following table details active related undertakings incorporated outside the United Kingdom where the Group ownership is less than 100%.

Country	Enitity name	Activity (1)	Accounting treatment (2)	Group interest%
Canada	1369202 Alberta ULC	BF	FC	51
Canada	Sempra Energy Trading (Calgary) ULC	BF	FC	51
China	Hua Ying Securities Company Ltd	BF	EAJV	33
Cyprus	Pharos Estates Ltd	OTH	EAA	49
France	Cinquième Lease G.I.E.	OTH	EAJV	33
France	Quatrième Lease G.I.E.	BF	EAJV	33
Germany	Argos Vermögensver-waltung GmbH	OTH	IA	40
Germany	BLIXA Elfte Vermögensver-waltung GmbH	OTH	IA	40
Germany	NASIL GmbH & Co. KG	BF	FC	94
Germany	TN Eagle 2 GmbH	BF	FC	99
Germany	TN Jet Stream 2 GmbH	BF	FC	99
Germany	TN Jet Stream GmbH	BF	FC	99
Republic of Ireland	Qulpic Ltd	BF	FC	67
Republic of Ireland	The Drive4Growth Company Ltd	OTH	IA	20
Republic of Ireland	Zrko Ltd	BF	FC	67
Jersey	Spring Allies Jersey Ltd	BF	IA	49
Netherlands	BNC IXAS SPC Holding B.V.	BF	IA	26
Netherlands	RBS Sempra Commodities Coöperatief W.A.	OTH	FC	51
Netherlands	RBS Sempra Commodities Holdings I B.V.	BF	FC	51
Norway	Norslundsskogen 5 KB	BF	FC	51
Poland	Wiśniowy Management sp. z o.o.	OTH	EAA	25
Sweden	Airside Properties AB	BF	EAA	50
Sweden	Bong Fastigheter KB	BF	FC	51
Sweden	Förvaltningsbolaget Klöverbacken Skola KB	BF	FC	51
Sweden	Optimus KB	BF	FC	51
Sweden	Stora Kvarnen KB	BF	FC	51
United States	Amtrust Acquisition LLC	BF	IA	24
United States	Sempra Energy Trading LLC	BF	FC	51

The following table details active related undertakings which are 100% owned by the Group but are not consolidated for accounting purposes (5).

Country	Entity Name	Activity (1)	Accounting treatment (1)	Notes
United States	West Granite Homes Inc.	OTH	NC	(6)

For notes to this table refer to page 264.

The following tables detail related undertakings that are not active.

Actively being dissolved				
Country	Entity name	Activity (1)	Accounting treatment (2)	Group interest %
Cayman Islands	Redshield Holdings Ltd	BF	FC	100
Germany	Greta Film Investition GmbH & Co. KG	BF	IA	25
Guernsey	Adam & Company International Ltd	BF	FC	100
Republic of Ireland	Danroc Ltd	OTH	FC	100
Republic of Ireland	First Active Investments No. 3 Ltd	BF	FC	100
Republic of Ireland	First Active Nominees Ltd	OTH	FC	100
Republic of Ireland	First Active Property Investments Ltd	OTH	FC	100
Republic of Ireland	GRG Real Estate Asset Management (Republic of Ireland) Ltd	BF	FC	100
Republic of Ireland	Meritvale Ltd	OTH	FC	100
Republic of Ireland	NatWest Holdings (Ireland)	BF	FC	100
Republic of Ireland	The Royal Bank of Scotland Finance (Ireland)	BF	FC	100
Republic of Ireland	UIF Finance Company	BF	FC	100
Republic of Ireland	Ulster Bank Group Treasury Ltd	OTH	FC	100
Republic of Ireland	Ulster Bank Investment Funds Ltd	OTH	FC	100
Republic of Ireland	Ulster International Finance	BF	FC	100
Mexico	RBS Sempra Energy Trading Mexico, S. de R.L. de C.V.	OTH	FC	51
Curaçao	RBSG Holdings N.V.	BF	FC	100
United Kingdom	Beauford PLC	OTH	FC	100
United Kingdom	Birchin Lane Nominees, Ltd	OTH	FC	100
United Kingdom	Burridge Holdings Ltd	BF	IA	40
United Kingdom	C W Nominees Ltd	OTH	FC	100
United Kingdom	Childs Nominees, Ltd	OTH	FC	100
United Kingdom	Drivefirst Ltd	OTH	FC	100
United Kingdom	Flexibuy Ltd	BF	FC	75
United Kingdom	GL Lease Company No.10 Ltd	OTH	FC	75
United Kingdom	GRG Real Estate Asset Management (Northern Ireland) Ltd	BF	FC	100
United Kingdom	Judges Postcards Ltd	OTH	IA	27
United Kingdom	Lombard Corporate Finance (1) Ltd	BF	FC	100
United Kingdom	Lombard Corporate Finance (December 2) Ltd	BF	FC	100
United Kingdom	Lombard Home Loans Ltd	OTH	FC	100
United Kingdom	Lombard Plant Finance Ltd	BF	FC	100
United Kingdom	National Provincial Bank Ltd	OTH	FC	100
United Kingdom	NatWest Corporate Services (Ireland)	BF	FC	100
United Kingdom	NatWest Industrial Finance Ltd	BF	FC	100
United Kingdom	NatWest Lease Management Ltd	BF	FC	100
United Kingdom	NatWest Stockbrokers Financial Services Ltd	OTH	FC	100
United Kingdom	NWM Property Advisory Ltd	OTH	FC	100
United Kingdom	Sampsons Ltd	OTH	IA	27
United Kingdom	The Mortgage Corp	OTH	FC	100
United Kingdom	The Royal Bank of Scotland Commercial Services Ltd	BF	FC	100
United Kingdom	Welsh Industrial Partnership (Nominee) Ltd	BF	FC	51
Virgin Islands, British	Minster Corporate Services Ltd	BF	FC	100

Dormant				
Country	Entity name	Activity (1)	Accounting treatment (2)	Group interest %
United Kingdom	Adam & Company (Nominees) Ltd	OTH	FC	100
Bahamas	CTB Ltd	BF	FC	100
Denmark	Nordisk Renting A/S	OTH	FC	100
Republic of Ireland	First Active plc	BF	FC	100
Jersey	Coutts (CI) Ltd	BF	FC	100
Jersey	National Westminster Bank Nominees (Jersey) Ltd	BF	FC	100
Jersey	RBS Cards Securitisation Funding Ltd	BF	FC	100

For notes to this table refer to page 264.

41.Related undertakings continued

Country	Entity name	Activity (1)	Accounting treatment (2)	Group interest %
Sweden	Nordisk Renting Facilities Management AB	OTH	FC	100
Sweden	Nordisk Renting Kapital AB	BF	FC	100
Sweden	Svenskt Energikapital AB	BF	FC	100
United Kingdom	Acre 146 Ltd	BF	FC	100
United Kingdom	Beveltop Ltd	BF	FC	100
United Kingdom	British Overseas Bank Nominees Ltd	OTH	FC	100
United Kingdom	Buchanan Holdings Ltd	BF	FC	100
United Kingdom	CNW Group Ltd	BF	FC	100
United Kingdom	CNW Nominees Ltd	OTH	FC	100
United Kingdom	Cornhill Holdings Ltd	BF	FC	100
United Kingdom	Coutts Group	OTH	FC	100
United Kingdom	CTL Nominees Ltd	OTH	FC	100
United Kingdom	District Bank Ltd	OTH	FC	100
United Kingdom	Dixon Motorcycle Holdings Ltd	BF	FC	100
United Kingdom	Dixon Vehicle Sales Ltd	OTH	FC	100
United Kingdom	Dormaco (No.12) Ltd	OTH	FC	100
United Kingdom	Doublemere Ltd	OTH	FC	100
United Kingdom	Dunfly Trustee Ltd	OTH	FC	100
United Kingdom	Ecosse Regeneration Ltd	OTH	FC	100
United Kingdom	Emperor Holdings Ltd	OTH	FC	100
United Kingdom	FIT Nominee Ltd	OTH	FC	100
United Kingdom	FIT Nominee 2 Ltd	BF	FC	100
United Kingdom	Freehold Managers (Nominees) Ltd	OTH	FC	100
United Kingdom	Glyns Nominees Ltd	OTH	FC	100
United Kingdom	Greenwich NatWest Ltd	BF	FC	100
United Kingdom	Honroe (UK) Ltd	BF	FC	100
United Kingdom	JCB Credit Ltd	OTH	FC	75
United Kingdom	JCB Finance Pension Ltd	BF	FC	88
United Kingdom	Landpower Leasing Ltd	BF	FC	75
United Kingdom	Lombard Bank	OTH	FC	100
United Kingdom	Lombard North Central Wheelease Ltd	BF	FC	100
United Kingdom	London Office Royal Bank of Scotland Nominees Ltd	OTH	FC	100
United Kingdom	Lothbury Property Trust Company Ltd	OTH	FC	100
United Kingdom	Marigold Nominees Ltd	OTH	FC	100
United Kingdom	Motorsport Dealers International Ltd	BF	FC	100
United Kingdom	N.C. Head Office Nominees Ltd	SC	FC	100
United Kingdom	N.C. Securities Ltd	OTH	FC	100
United Kingdom	National Westminster Ltd	BF	FC	100
United Kingdom	NatWest Aerospace Trust Company Ltd	BF	FC	100
United Kingdom	NatWest FIS Nominees Ltd	OTH	FC	100
United Kingdom	NatWest Invoice Finance Ltd	BF	FC	100
United Kingdom	NatWest Nominees Ltd	OTH	FC	100
United Kingdom	NatWest PEP Nominees Ltd	OTH	FC	100
United Kingdom	NatWest Security Trustee Company Ltd	OTH	FC	100
United Kingdom	North Central Finance Ltd	OTH	FC	100
United Kingdom	Pensman Nominees Ltd	OTH	FC	100
United Kingdom	Project & Export Finance (Nominees) Ltd	OTH	FC	100
United Kingdom	R.B.S. Property (Greenock) Ltd	OTH	FC	100
United Kingdom	RB Investments 5 Ltd	BF	FC	100
United Kingdom	RBS CIF Trustee Ltd	OTH	FC	100
United Kingdom	RBS Investment Executive Ltd	OTH	NC	100
United Kingdom	RBS Pension Trustee Ltd	OTH	NC	100
United Kingdom	RBS Residential Venture No.2 Ltd	OTH	FC	100
United Kingdom	RBS Retirement Savings Trustee Ltd	OTH	FC	100
United Kingdom	RBS Secretarial Services Ltd	OTH	FC	100
United Kingdom	RBS Shelf Nominees Ltd	BF	FC	100
United Kingdom	RBS Trustees Ltd	BF	FC	100
United Kingdom	RBSG Collective Investments Nominees Ltd	BF	FC	100
United Kingdom	Riossi Motorcycles Ltd	OTH	FC	100
United Kingdom	RoboScot (64) Ltd	OTH	FC	100
United Kingdom	Rover Finance Holdings Ltd	BF	FC	100

For notes to this table refer to page 264.

41.Related undertakings continued

Country	Entity name	Activity (1)	Accounting treatment (2)	Group interest %
United Kingdom	Rover Finance Ltd	BF	FC	100
United Kingdom	Royal Bank Business Asset Finance Ltd	BF	FC	100
United Kingdom	Royal Bank Insurance Consultants Ltd	BF	FC	100
United Kingdom	RoyScot Auto Credit Ltd	BF	FC	100
United Kingdom	RoyScot Contracts Ltd	OTH	FC	100
United Kingdom	RoyScot Industrial Leasing Ltd	BF	FC	100
United Kingdom	RoyScot Leasing Ltd	BF	FC	100
United Kingdom	RoyScot Motor Finance Ltd	BF	FC	100
United Kingdom	RoyScot Vehicle Contracts Ltd	OTH	FC	100
United Kingdom	Sixty Seven Nominees Ltd	OTH	FC	100
United Kingdom	Strand Nominees Ltd	BF	FC	100
United Kingdom	Syndicate Nominees Ltd	OTH	FC	100
United Kingdom	The Financial Trading Company Ltd	BF	FC	100
United Kingdom	The National Bank Ltd	OTH	FC	100
United Kingdom	The Royal Bank of Scotland (1727) Ltd	BF	FC	100
United Kingdom	Van Finance Ltd	BF	FC	80
United Kingdom	Ventus Investments Ltd	OTH	FC	100
United Kingdom	W.G.T.C.Nominees Ltd	OTH	FC	100
United Kingdom	Westments Ltd	BF	FC	100
United Kingdom	Westminster Bank Ltd	OTH	FC	100
United Kingdom	Williams & Glyn Holdings Ltd	BF	FC	100
United Kingdom	Williams & Glyn's Bank Ltd	OTH	FC	100
United Kingdom	Williams & Glyn's Trust Company Ltd	OTH	FC	100

In Administration

Country	Entity name	Activity (1)	Accounting treatment (2)	Group interest %
United Kingdom	Adam & Company Second General Partner Ltd	BF	IA	50
United Kingdom	Big Beat Holdings Ltd	OTH	IA	42
United Kingdom	Care At Home (Wales) Ltd	OTH	IA	25
United Kingdom	VMG Foods Ltd	OTH	IA	40

Notes:
(1) Activity:
Banking and Financial institution - BF
Credit institution – CI
Service company - SC
Other/non-financial - OTH
(2) Accounting treatment:
Equity accounting - Associate - EAA
Equity accounting - Joint Venture - EAJV
Fully consolidated - FC
Investment Accounting - IA
Not consolidated - NC
(3) The Group is interested in 45% of the voting rights and 42% of the economic rights.
(4) Related undertaking consolidated because RBS controls the company by virtue of contractual agreements.
(5) Related undertaking not consolidated as it is not controlled by the Group.
(6) Related undertaking owned for the benefit of Group pension schemes.

Financial summary

The Group's financial statements are prepared in accordance with IFRS. Selected data under IFRS for each of the last five years are presented below.

Summary consolidated income statement	2015 £m	2014 £m	2013 £m	2012 £m	2011 £m
Net interest income	8,408	8,866	8,630	8,586	9,221
Non-interest income (1,2,3)	3,743	5,752	8,125	6,676	9,319
Total income	12,151	14,618	16,755	15,262	18,540
Operating expenses (4)	(16,141)	(13,552)	(15,985)	(14,616)	(13,523)
(Loss)/profit before impairment losses	(3,990)	1,066	770	646	5,017
Impairment releases/(losses)	837	1,337	(8,137)	(4,945)	(6,547)
Operating (loss)/profit before tax	(3,153)	2,403	(7,367)	(4,299)	(1,530)
Tax credit/(charge)	29	(2,033)	(307)	(51)	(519)
(Loss)/profit from continuing operations	(3,124)	370	(7,674)	(4,350)	(2,049)
Profit/(loss) from discontinued operations, net of tax (5)	1,538	(3,486)	410	490	303
Loss for the year	(1,586)	(3,116)	(7,264)	(3,860)	(1,746)
Attributable to:					
Non-controlling interests	320	57	(13)	19	(8)
Preference shareholders	44	61	58	58	58
Ordinary shareholders	(1,950)	(3,234)	(7,309)	(3,937)	(1,796)

Notes:
(1) Includes loss on strategic disposals of £159 million (2014 - £1 million gain; 2013 - £161 million gain; 2012 - £185 million gain; 2011 - £57 million loss).
(2) Includes loss on redemption of own debt of £263 million (2014 - £6 million gain; 2013 - £162 million gain; 2012 - £454 million gain; 2011 - £255 million gain).
(3) Includes own credit adjustments of £327 million gain (2014 - £12 million loss; 2013 - £25 million loss; 2012 - £3,904 million loss; 2011 - £797 million gain).
(4) Includes write down of goodwill of £498 million (2014 - £130 million; 2013 - £18 million; 2012 - £105 million; 2011 - nil).
(5) Includes a gain of £1,130 million relating to the sell-down of Citizens (2014 - £3,994 million loss).

Summary consolidated balance sheet	2015 £m	2014* £m	2013* £m	2012* £m	2011* £m
Loans and advances	364,799	421,530	505,583	576,904	586,539
Debt securities and equity shares	81,096	89,477	108,974	150,457	180,903
Derivatives and settlement balances	267,191	359,292	295,037	450,818	539,709
Other assets	99,105	175,083	110,284	106,073	125,641
Total assets	812,191	1,045,382	1,019,878	1,284,252	1,432,792
Owners' equity	41,853	45,303	48,702	59,249	61,689
Non-controlling interests	54	2,385	79	137	128
Subordinated liabilities	27,030	30,469	33,134	33,851	32,324
Deposits	416,168	458,849	537,467	621,457	581,485
Derivatives, settlement balances and short positions	279,739	378,309	319,382	469,458	575,060
Other liabilities	47,347	130,067	81,114	100,100	182,106
Total liabilities and equity	812,191	1,045,382	1,019,878	1,284,252	1,432,792

*Restated - refer to page 148 for further details.

Other contractual cash obligations

The table below summarises the Group's other contractual cash obligations by payment date.

	Group					
2015	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Operating leases	60	172	421	338	692	1,314
Contractual obligations to purchase goods or services	81	221	570	570	—	—
	141	393	991	908	692	1,314
2014						
Operating leases	62	175	424	360	695	1,415
Contractual obligations to purchase goods or services	104	285	703	734	1	—
	166	460	1,127	1,094	696	1,415

	Bank					
2015	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Operating leases	36	105	265	236	505	902
Contractual obligations to purchase goods or services	70	212	566	566	—	—
	106	317	831	802	505	902
2014						
Operating leases	38	107	265	239	510	982
Contractual obligations to purchase goods or services	92	273	696	728	—	—
	130	380	961	967	510	982

Cross border exposures

Cross border exposures are loans and advances including finance leases and instalment credit receivables and other monetary assets, such as debt securities and net derivatives, including non-local currency claims of overseas offices on local residents.

The Group monitors the geographical breakdown of these exposures based on the country of domicile of the borrower or guarantor of ultimate risk. Cross border exposures exclude exposures to local residents in local currencies.

The table below sets out the Group's cross border exposures greater than 0.5% of the Group's total assets. None of these countries have experienced repayment difficulties that have required restructuring of outstanding debt

2015	Government £m	Banks £m	Other £m	Total £m	Short positions £m	Net of short positions £m
United States	10,971	3,528	8,895	23,394	287	23,107
France	6,221	10,794	2,626	19,641	1,778	17,863
Germany	9,574	4,211	1,565	15,350	3,272	12,078
Netherlands	3,820	984	7,097	11,901	786	11,115
Japan	7,172	2,442	211	9,825	—	9,825
Italy	4,946	954	687	6,587	3,229	3,358
Spain	989	730	1,690	3,409	535	2,874
Republic of Ireland	185	768	1,453	2,406	68	2,338
2014						
United States	393	2,500	18,231	21,124	7,029	14,095
France	7,222	11,654	4,234	23,110	2,226	20,884
Germany	12,837	5,045	2,437	20,319	2,166	18,153
Netherlands	5,050	1,037	6,891	12,978	1,391	11,587
Japan	3,093	3,623	2,125	8,841	66	8,775
Italy	3,379	989	766	5,134	3,029	2,105
Spain	772	913	2,442	4,127	565	3,562
Republic of Ireland	180	1,454	1,793	3,427	11	3,416
2013						
United States	7,592	1,917	24,354	33,863	7,984	25,879
France	4,432	10,033	4,182	18,647	2,352	16,295
Germany	11,975	2,521	4,802	19,298	4,440	14,858
Netherlands	4,979	1,548	5,927	12,454	1,192	11,262
Japan	34	4,866	1,876	6,776	2,556	4,220
Italy	4,922	635	1,089	6,646	3,302	3,344
Spain	1,417	2,813	3,486	7,716	801	6,915
Republic of Ireland	30	2,554	2,698	5,282	51	5,231

Risk factors

Set out below are certain risk factors that could adversely affect the Group's future results, its financial condition and prospects and cause them to be materially different from what is expected. The Group is the principal operating subsidiary of The Royal Bank of Scotland Group plc ("RBSG" and, together with its subsidiaries, the "RBS Group"). Accordingly, the risk factors described below which relate to RBSG and the RBS Group will also be applicable to the Bank and the Group and the occurrence of any such risks could have a material adverse effect on the Group's business, reputation, results of operations, financial condition, cash flows or future prospects. The factors discussed below and elsewhere in this report should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties facing the Group.

The RBS Group is subject to a number of legal, regulatory and governmental actions and investigations. Unfavourable outcomes in such actions and investigations could have a material adverse effect on the RBS Group's operations, operating results, reputation, financial position and future prospects.

In the past eight years, the RBS Group has dramatically downsized and simplified the scale and complexity of its operations as compared to its operations preceding and during the financial crisis. However, the RBS Group's operations remain diverse and complex, and the RBS Group operates in legal and regulatory environments that expose it to potentially significant litigation, civil and criminal regulatory and governmental investigations and other regulatory risk. The RBS Group has settled a number of legal and regulatory investigations over the past several years but continues to be, and may in the future be, involved in a number of legal and regulatory proceedings and investigations in the UK, the US, Europe and other jurisdictions.

The RBS Group is involved in ongoing reviews, investigations and proceedings (both formal and informal) by governmental law enforcement and other agencies and litigation (including class action litigation), relating to, among other matters, the offering of securities, conduct in the foreign exchange market, the setting of benchmark rates such as LIBOR and related derivatives trading, the issuance, underwriting, and sales and trading of fixed-income securities (including structured products and government securities), product mis-selling, customer mistreatment (including alleged mistreatment of small and medium enterprises by RBS's Global Restructuring Group, as alleged in the November 2013 report by Lawrence Tomlinson), anti-money laundering, sanctions, and various other compliance issues. In the US, ongoing matters include various civil and criminal federal and state investigations relating to the securitisation of mortgages, as well as the trading of various forms of asset-backed securities. The RBS Group continues to cooperate with governmental and regulatory authorities in these and other investigations and reviews. For more detail on certain of the RBS Group's ongoing legal, governmental and regulatory proceedings, see pages 234 to 244.

Legal, governmental and regulatory proceedings and investigations are subject to many uncertainties, and their outcomes, including the timing and amount of fines or settlements, which may be material, are often difficult to predict, particularly in the early stages of a case or investigation. Settlements, resolutions and outcomes in relation to ongoing investigations may result in material financial fines or penalties, non-monetary penalties, ongoing commitments, restrictions upon or revocation of regulatory permissions and licences and other collateral consequences and may prejudice both contractual and legal rights otherwise available to the RBS Group and the outcome of on-going claims against the RBS Group may give rise to additional legal claims being asserted against the RBS Group, any of which outcomes could materially adversely impact the RBS Group's capital position and prospects. Monetary penalties and other outcomes could be materially in excess of provisions, if any, made by the RBS Group. It is expected that the RBS Group will continue to have a material exposure to litigation and governmental and regulatory proceedings and investigations relating to legacy issues in the medium term. Adverse outcomes or resolution of current or future regulatory, governmental or law enforcement proceedings or adverse judgements in litigation could result in restrictions or limitations on the RBS Group's and/or the Group's operations, adversely impact the RBS Group's strategic programme or have a material adverse effect on the RBS Group's and/or the Group's reputation, results of operations, capital position and prospects.

The RBS Group may be required to make new or increase existing provisions in relation to existing or future legal proceedings, investigations and governmental and regulatory matters which may be substantial, including with respect to current matters in relation to which the RBS Group has not yet recognised legal provisions. In 2015, the RBS Group booked a provision of £334 million in respect of foreign exchange trading-related investigations. In 2015 the RBS Group booked an additional £2.1 billion related principally to mortgage-backed securities ("MBS") litigation in the US (resulting in total provisions made for this matter of £3.8 billion, of which £0.1 billion had been utilised at 31 December 2015). No provisions have been made in relation to resolving the ongoing US Department of Justice and various US State Attorneys General investigations into MBS-related conduct matters. The costs of resolving these investigations and the costs (beyond existing provisions) of resolving MBS litigation in the US could individually or in aggregate prove to be substantial. The RBS Group also booked in 2015 additional provisions of £600 million for Payment Protection Insurance, resulting in total provisions made for this matter of £4.3 billion, of which £3.3 billion had been utilised by 31 December 2015 and there remains a risk of future provisions and costs.

The provision for interest rate hedging products redress and administration costs was also increased by £68 million (net of releases) in 2015, with total provisions relating to this matter totalling £1.5 billion, of which £1.35 billion had been utilised at 31 December 2015. Significant new provisions or increases in existing provisions relating to legal proceedings, investigations and governmental and regulatory matters may have a material adverse effect on the RBS Group's and/or the Group's financial condition and results of operations as well as their reputation.

The RBS Group is subject to political risks

The European Union Referendum Act 2015 requires the UK government to hold a referendum on the UK's membership of the European Union, the date of which has been scheduled for 23 June 2016. The outcome of the EU referendum and consequences for the UK could significantly impact the environment in which the RBS Group, its customers and investors operate, introducing significant new uncertainties in financial markets, as well as the legal and regulatory requirements and environment to which the RBS Group, its customers and investors are subject. Uncertainty as to the outcome of the referendum will therefore lead to additional market volatility and is likely to adversely impact customer and investor confidence prior to the vote.

In the event of a result supporting the UK's exit from the European Union, the lack of precedent means that it is unclear how the UK's access to the EU Single Market and the wider trading, legal and regulatory environment would be impacted and hence how this would affect the RBS Group, its customers and investors. During a transitional period, when the terms of the exit would be negotiated, or beyond, the related uncertainty could have a material adverse effect on any of the RBS Group's and Group's business, financial condition, credit ratings and results of operations. A vote supporting the UK's exit from the European Union may also give rise to further political uncertainty regarding Scottish independence.

Pursuant to the State Aid Commitment Deed and its strategic programme, the RBS Group is in the process of separating Williams & Glyn with a view to fully divesting the business by the end of 2017. The scale and complexity of this process and the diversion of RBS Group resources required to support it, or delays in meeting the divestment deadline, could have a material adverse effect on the RBS Group's and the Group's operations, operating results, financial position and reputation.

The RBS Group has met all of the divestment commitments contained within the set of conditions upon which state aid approval was received from the European Commission for the financial assistance provided to the RBS Group by the UK Government in December 2008, save for the divestment of the RBS Group's RBS branches in England and Wales, NatWest branches in Scotland, direct SME banking and certain mid-corporate customers as a separate business under the Williams & Glyn brand ("Williams & Glyn").

In connection with the receipt of such aid, the RBS Group entered into a state aid commitment deed with HM Treasury (as amended from time to time, the "State Aid Commitment Deed"). In light of its obligations under the State Aid Commitment Deed to fully divest Williams & Glyn by the end of 2017, the RBS Group has been actively seeking to fully divest Williams & Glyn in accordance with this timetable. Due to significant execution challenges, the separation of the Williams & Glyn business from the RBS Group will now not be until after Q1 2017, as previously announced. The RBS Group remains committed to full divestment by the end of 2017, although it continues to face significant challenges and risks in separating the Williams & Glyn business, some of which may only emerge as various separation process phases are progressed. The complexities or delays in separation may impact the RBS Group's ability to meet the divestment deadline and could result in the RBS Group adopting an alternative divestment structure to either of the current plans for divestment.

There is potential for non-compliance if the RBS Group fails to meet this deadline, which might result in the RBS Group breaching the terms of the State Aid Commitment Deed and might constitute a misuse of state aid. In such circumstances, a divestiture trustee may be appointed, with the mandate to complete the disposal at no minimum price. This may adversely affect the attractiveness of, and result in additional execution risks in respect of the sale of, Williams & Glyn. Furthermore, a failure to comply with the terms of the State Aid Commitment Deed could result in the imposition of additional remedies or limitations on the RBS Group's operations, additional supervision by the RBS Group's regulators, and loss of investor confidence, any of which could have a material adverse impact on the RBS Group and/or the Group. Delays in execution may also impact the RBS Group's ability to carry out its strategic programme and implement mandatory regulatory requirements, including the UK ring fencing regime. Such risks will increase in line with any additional delays.

The availability and interest of buyers or investors for Williams & Glyn or the ability of the RBS Group to divest the business on commercially attractive terms is not certain. In particular, Williams & Glyn is a complex business and unforeseen difficulties in integrating the business with that of any buyer could deter potential buyers from bidding for the business or completing the sale. In addition, the number of potential bidders with synergy potential or strategic interests may be limited and such investors may value the business below what the RBS Group considers to be the fair value of the Williams & Glyn business.

The divestment of the Williams & Glyn business from the RBS Group requires significant structural, governance and IT changes, which are complex to implement and will impact the RBS Group's customers, operations and controls. In particular, a key component of the current separation plan is the successful migration of the Williams & Glyn business to a stand-alone and operational technology platform.

Given the current interconnectedness of the Williams & Glyn business and other parts of the RBS Group and in order to seek to meet the deadlines for divestment, this process will necessarily divert management and personnel resources from the effective conduct of the RBS Group's operations and jeopardise the delivery and implementation of a number of other significant change projects resulting from mandatory regulatory developments or as part of its strategic programme. In addition, the execution of the separation and divestment will result in significant costs. There are currently approximately 6,000 employees (FTE) engaged on the project and total costs incurred to 31 December 2015 relating to the separation and divestment of Williams & Glyn were £1.2 billion and are expected to increase through to completion. Although the RBS Group is committed to achieving the separation and divestment in the most cost-efficient manner, due to unforeseen complexities and factors outside of the RBS Group's control, costs could be materially higher than currently contemplated.

Furthermore, an essential precondition for a trade sale or IPO of Williams & Glyn will be the granting of a banking licence by the PRA, an application for which was submitted in September 2015, which in turn will depend, among other things, on demonstrating progress on the separation. Delays in obtaining the licence may impact the sale process and buyer confidence or the RBS Group's ability to meet the prescribed deadlines for divestment. As a direct consequence of the divestment of Williams & Glyn, the RBS Group will lose existing customers, deposits and other assets. It may also lose the potential for realising additional associated revenues and margins, or cost savings that it otherwise might have achieved. The RBS Group will also be unable to fully reduce its shared central costs in proportion to the scale of reduction in income resulting from the divestment of Williams & Glyn. The RBS Group's financial condition may also be exposed to risk with respect to the control, management and results of operations of Williams & Glyn during a transitional period.

The divestment may also have a negative impact on the RBS Group's competitive position, including through the emergence of a new competitor. Depending on the form in which Williams & Glyn is divested, the RBS Group may agree or be required to provide services for, or other forms of support (financial or otherwise) to, Williams & Glyn, which may result in reputational and financial exposure for the RBS Group and may require significant attention from the RBS Group's senior management, in particular in respect of managing conflicts of interests and confidentiality of data.

The RBS Group has been, and will remain, in a period of major restructuring through to 2019, which carries significant execution and operational risks, and there can be no assurance that the final results will be successful and that the RBS Group will be a viable, competitive, customer-focussed and profitable banking group.

In the first quarter of 2015, the RBS Group articulated a new strategy focussed on the growth of its strategic operations in UK Personal & Business Banking and Commercial & Private Banking and the further restructuring of its Corporate and Institutional Banking ("CIB") business to focus mainly on UK and Western European corporate and financial institutions. It also announced the acceleration of the run-down of certain of its operations, businesses and portfolios in order to reduce risk-weighted assets as well as the scope and complexity of its activities. In 2015, the RBS Group also continued the run-down of the higher risk and capital intensive assets in RBS Capital Resolution ("RCR"), which has now been merged into Capital Resolution, and strengthened the RBS Group's capital position, including through the full divestment of the RBS Group's interest in Citizens Financial Group ("CFG"), which were key goals of its previous strategic plan. Finally, the RBS Group remains focussed on meeting its returns and efficiency targets (including cost reductions) as well as improving customer experience and employee engagement.

This strategy is intended to leave the RBS Group better positioned for the implementation of the UK ring-fencing regime. The RBS Group's strategy is also focussed on strengthening its overall capital position. During the restructuring period and until the implementation of the UK ring-fencing regime in 2019, the RBS Group has lifted its capital targets and currently aims for a CET1 ratio at or over 13%.

Implementing the RBS Group's current strategic programme, including the restructuring of its CIB business, will require further material changes to be implemented within the RBS Group over the medium term at the same time that it will also be implementing structural changes to comply with the UK ring-fencing regime and divesting Williams & Glyn. The RBS Group expects this restructuring period to be disruptive and likely to increase operational and people risks for the RBS Group and may divert management resources from the conduct of the RBS Group's operations and development of its business.

The RBS Group may not be able to successfully implement any part of its strategic programme in the time frames contemplated or at all, and, as a result, the RBS Group may not be able to achieve its stated capital targets or its strategic objectives. The RBS Group's strategic programme comprises a number of different actions and initiatives, any of which could fail to be implemented due to operational or execution issues. Implementation of the RBS Group's strategic programme is expected to result in significant costs, which could be materially higher than currently contemplated, including due to material uncertainties and factors outside of the RBS Group's control.

Although one of the objectives of the RBS Group's strategic programme is to achieve a medium-term reduction in annual underlying costs (excluding restructuring and conduct-related charges), this level of cost saving may not be achieved within the planned timescale or at any time. Such risks are linked to and additional to the risks relating to the implementation of the UK ring-fencing regime and the divestment of Williams & Glyn, and will be increased by issues or delays in their implementation, in particular delays in the separation and divestment of Williams & Glyn.

On completion of the implementation of its strategic programme and the UK ring-fencing regime in 2019, the RBS Group's businesses will be primarily concentrated in the UK and Western Europe, and therefore its potential for profitability and growth will be largely dependent on its success with its retail and SME customers in the UK. Due to the changed nature of the RBS Group's business model, future levels of revenue may not be achieved in the timescale envisaged or at any time. In addition, there can be no guarantee that the new business model defined for CIB will result in a sustainable or profitable business. As a result, in addition to the execution risks associated with the implementation of its strategic programme and of the UK ring-fencing regime, there can be no assurance that even if the RBS Group executes its strategic programme, it will prove to be a successful strategy or that the restructured RBS Group, on completion of these restructuring measures, will be a viable, competitive, customer-focussed and profitable banking group.

Implementation of the ring-fencing regime in the UK which began in 2015 and must be completed by 1 January 2019 will result in material structural changes to the RBS Group's business. These changes could have a material adverse effect on the RBS Group and the Group.

The UK Government's White Paper on Banking Reform published in September 2012 outlined material structural reforms for the UK banking industry. The implementation of the "ring-fencing" of retail banking operations was introduced under the UK Financial Services (Banking Reform) Act 2013 (the "Banking Reform Act 2013") and adopted through secondary legislation (the "UK ring-fencing regime"). These reforms form part of a broader range of structural reforms of the banking industry seeking to improve the resilience and resolvability of banks and which range from structural reforms (including ring-fencing) to the implementation of a new recovery and resolution framework (which in the UK will incorporate elements of the ring-fencing regime). See "*The RBS Group and its subsidiaries are subject to a new and evolving framework on recovery and resolution, the impact of which remains uncertain and which may result in additional compliance challenges and costs*."

The Prudential Regulation Authority ("PRA") is carrying out consultations with the RBS Group and other affected UK banks and is expected to publish the majority of its final rules and supervisory statements during the first half of 2016.

The PRA has indicated that the implementation of the UK ring-fencing regime may be further amended in light of any finalised EU proposals for the mandatory separation of proprietary trading and related trading activities which are currently being considered by the European Parliament and the European Council. A preliminary plan outlining the RBS Group's anticipated legal and operating structure under the new regime was submitted to the PRA and the Financial Conduct Authority ("FCA") by the deadline set by the regulators of 6 January 2015. On 29 January 2016, the RBS Group submitted an update to its draft ring-fencing plans to the regulators.

The RBS Group has identified a number of material operational, execution and legal risks associated with the implementation of the UK ring-fencing regime. These are in addition to the uncertainty associated with starting to plan and prepare for implementation before final rules and guidance are in place or before the RBS Group applies for or obtains certain waivers or modifications (as envisaged under the rules), which it expects to require. These risks may be exacerbated by the RBS Group's other ongoing restructuring efforts, including, in particular, the separation of the Williams & Glyn business, and new and developing legal requirements relating to the regulatory framework for banking resolution.

- The RBS Group intends to establish a ring-fenced bank sub-group ("RFB") organised under an intermediate holding company for its UK-focussed banking services while the non-ring-fenced RBS Group entities ("NRFBs") will hold the RBS Group's remaining trading activities, the operations of RBS International and all non-EEA branches and subsidiaries and some banking activities that are not permitted activities for the RFB. The establishment of the RFB and the NRFBs will have a material impact on how the RBS Group conducts its business and require a significant legal and organisational restructuring of the RBS Group and the Group and the transfer of large numbers of assets, liabilities and customers between legal entities and the realignment of employees, (which may be subject to consultation with employee representatives) and will be contingent upon court, regulatory or board approvals. The RBS Group is unable to predict how some customers may react to the required changes, including for some customers a requirement to deal with both the RFB and NRFBs to obtain the full range of products and services. The migration of some customers is also dependent on the completion of the technical separation of Williams & Glyn from the RBS Group.
- As part of the establishment of the RFB, the RFB will need to operate independently from the NRFBs and material changes to the existing corporate governance structure will need to be put in place by the RBS Group to ensure the RFB's independence and the RBS Group cannot predict the extent of the associated increase in overhead and compliance costs.

- In order to comply with the requirements of the UK ring-fencing regime, the RBS Group will need to revise its operations infrastructure so as to comply with the shared services, independence and resolvability requirements set out in the UK ring-fencing rules, including in areas such as information technology ("IT") infrastructure, human resources and critical service providers. Arrangements between RFB and NRFBs entities will also need to be reviewed in light of these requirements and the requirement that all such transactions take place on an arm's-length basis.
- The implementation of the UK ring-fencing regime will significantly impact the management of the RBS Group's treasury operations, including internal and external funding arrangements and may impact the credit ratings of some of the RFB or NRFBs entities, including the Bank. Reliance on intra-group exemptions in relation to the calculation of risk-weighted assets and large exposures may not be possible between the RFB and NRFB entities. Intra-group distributions (including payments of dividends) between RFB and NRFB entities (which will include the RBS Group parent company) will also be subject to certain limitations. The RFB sub-group will have to meet prudential requirements, including Pillar 2A requirements and the UK's Systemic Risk Buffer, at RFB sub-group level, in addition to meeting existing requirements applied on an individual entity basis (where applicable). The potential loss of intra-group exemptions and the application of additional prudential requirements could result in increased capital requirements and related compliance costs.
- In order to comply with the UK ring-fencing regime, from 2026 it will not be possible for the RFB and the NRFBs to participate in the same defined benefit pension plan. As a result, it will be necessary for either the RFB or NRFBs to leave the current pension plan and the costs of separation may be material and may trigger certain legal and regulatory obligations, including possibly increasing annual cash contributions required to be made into the RBS Group's pension plans. Such separation may also result in additional or increased cash contributions in the event the pension trustees determine that the employer covenant has been weakened as a result of such separation.
- The RBS Group will also need to evaluate, among other things, any accounting consequences resulting from the restructuring as well as any tax costs, the tax attributes of each of the RFB and NRFBs and the ability to transfer tax losses between RFB and NRFB entities. Transfers of assets that have related hedging arrangements may result in adverse operational, financial or accounting consequences if the transfer is not consistent with the unaffected continuation of such hedging arrangements.

The steps required to implement the UK ring-fencing regime within the RBS Group to comply with the new rules and regulations are extraordinarily complex and will take an extended period of time to plan, execute and implement and entail significant costs and operational risks.

These operational risks are heightened as the UK ring-fencing regime will be implemented during a period of significant business restructuring, which is expected to be dependent on the completion of the technical separation of Williams & Glyn from the RBS Group.

Although final implementation is not required until 1 January 2019, there is no certainty that the RBS Group will be able to complete the legal restructuring and migration of customers on time or in accordance with future rules and the consequences of non-compliance are currently uncertain. Conducting the RBS Group's operations in accordance with the new rules may result in additional costs (transitional and recurring) following implementation and impact the RBS Group's and/or the Group's profitability. As a result, the implementation of the UK ring-fencing regime could have a material adverse effect on the RBS Group's and/or the Group's reputation, results of operations, financial condition and prospects.

Operational risks are inherent in the RBS Group's businesses and these risks could increase as the RBS Group implements its strategic programme, the UK ring-fencing regime and the divestment of Williams & Glyn.

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people or systems, or from external events, including legal risk. The RBS Group has complex and geographically diverse operations and operational risk and losses can result from IT failures, internal and external fraud, errors by employees or third parties, failure to document transactions properly or to obtain proper authorisations, failure to comply with applicable regulatory requirements and conduct of business rules (including those arising out of anti-bribery, anti-money laundering and antiterrorism legislation, as well as the provisions of applicable sanctions programmes), equipment failures, financial reporting errors or deficiencies, business continuity and data security system failures, information security threats or deficiencies, including cyber risk, natural disasters or the inadequacy or failure of systems and controls, including those of the RBS Group's suppliers or counterparties.

Operational risks will be heightened as a result of the restructuring of the RBS Group relating to the implementation of its strategic programme. The implementation of the UK ring-fencing regime, the divestment of Williams & Glyn and the restructuring of the CIB business carry significant execution and delivery risk, are being delivered against the backdrop of ongoing cost challenges and will put significant pressure on the RBS Group's ability to maintain effective internal controls. Although the RBS Group has implemented risk controls and loss mitigation actions and significant resources and planning have been devoted to plans to mitigate operational risk associated with the RBS Group's activities as well as the implementation of the RBS Group's strategic programme, the UK ring-fencing regime, and the divestment of Williams & Glyn, it is not possible to be certain that such actions have been or will be effective in controlling each of the operational risks faced by the RBS Group.

Ineffective management of operational risks could have a material adverse effect on the RBS Group's and/or the Group's business, financial condition and results of operations.

The RBS Group's businesses and performance can be negatively affected by actual or perceived global economic and financial market conditions and other global risks and the RBS Group will be increasingly impacted by developments in the UK as its operations become increasingly concentrated in the UK.

On completion of the restructuring of the RBS Group relating to the implementation of its strategic programme and the UK ring-fencing regime, its business focus will be primarily in the UK and Western Europe. Although the prospects for the UK and the United States remain the strongest among the G-7 in 2016 and Ireland's economy continues to improve, actual or perceived difficult global economic conditions, failure to meet economic growth projections, particularly in the UK and the RBS Group's other key markets, regulators' concerns relating to the UK buy-to-let market and possible restrictions on mortgage lending as well as increased competition, particularly in the UK, would create challenging economic and market conditions and a difficult operating environment for the RBS Group's businesses.

In addition, a number of European economies have not yet recovered from the effects of the financial crisis and consensus forecasts of growth in 2016 and 2017 for some of the largest European economies such as France and Italy remain weak and the economic recovery of Greece and other European economies remains uncertain. As a result, concerns relating to sovereign default, exit or breakup of the eurozone, and the direct and indirect impact of such events on the UK and other European economies, remain.

The RBS Group's businesses and many of its customers are, and will continue to be, affected by global economic conditions, perceptions of those conditions and future economic prospects, in particular insofar as they impact the UK economy. The outlook for the global economy over the near to medium-term remains uncertain due to a number of factors including: major geopolitical instability, historically depressed oil and commodity prices, concerns around global growth and liquidity, uncertainty relating to the scope and timing of interest rate rises against a backdrop of historically high sovereign and household borrowing levels and stagnant inflation or deflation. In particular, slowing growth and high debt levels in emerging market economies to which the RBS Group is exposed (including those economies to which the RBS Group remains exposed pending the exit of certain of its businesses and which include China, India, Saudi Arabia and Russia) remains an area of concern and a further slowing of emerging country economic growth or recession, appreciation of the US dollar, new or extended economic sanctions or increased financing needs as existing debt matures, could impact the RBS Group directly by resulting in credit losses and indirectly by further impacting global economic growth and financial markets. The RBS Group's businesses and performance are also affected by financial market conditions.

Financial markets, in particular equity and commodity markets, experienced considerable volatility in late 2014 and in 2015 which has continued into 2016 and has translated in a downward trend in financial markets which has in turn resulted in significant value destruction.

These trends are attributable to many of the factors noted above as well as significant downward movements in world markets, especially China, and revised projections for Chinese and emerging market economic growth during the second half of 2015 and the beginning of 2016. Financial markets also were and will likely continue to be impacted by the uncertainty as to how economies and counterparties will be affected, directly or indirectly, by the impact and timing of monetary policy measures adopted by the Bank of England, the European Central Bank ("ECB"), the US Federal Reserve and other central banks, including the Bank of Japan. While the ECB has been implementing a quantitative easing programme since January 2015 designed to improve confidence in the eurozone and encourage more private bank lending, there remains considerable uncertainty as to whether such measures have been or will be sufficient or successful.

The challenging operating environment for the RBS Group's businesses, created by uncertain economic and market conditions, is characterised by:

- prolonged periods of low interest rates resulting from ongoing central bank measures to foster economic growth which constrain, through margin compression and low returns on assets, the interest income earned by the RBS Group;
- budgetary concerns affecting sovereign credit ratings and impacting consumer confidence and spending and business confidence;
- reduced activity levels, additional write-downs and impairment charges and lower profitability, which either alone or in combination with regulatory changes or the activities of other market participants may restrict the ability of the RBS Group to access capital, funding and liquidity; and
- the risk of increased volatility in yields and asset valuations as central banks accelerate looser monetary policies (such as in Japan or Europe) or tighten or unwind historically unprecedented loose monetary policy or extraordinary measures (such as in the US).

Developments relating to current economic conditions and instability in financial markets, including those discussed above, could have a material adverse effect on the RBS Group's and/or the Group's business, financial condition, results of operations and prospects.

In addition, the RBS Group is exposed to risks arising out of geopolitical events, such as trade barriers, exchange controls and other measures taken by sovereign governments that can hinder economic or financial activity levels. Furthermore, unfavourable political, military or diplomatic events, armed conflict, pandemics and terrorist acts and threats, and the responses to them by governments, could also adversely affect economic activity and have an adverse effect upon the RBS Group's and/or the Group's business, financial condition and results of operations.

Changes in interest rates, foreign exchange rates, credit spreads, bond, equity and commodity prices, basis, volatility and correlation risks and other market factors have significantly affected and will continue to affect the RBS Group's business and results of operations.

Some of the most significant market risks that the RBS Group faces are interest rate, foreign exchange, credit spread, bond, equity and commodity prices and basis, volatility and correlation risks. Monetary policy has been highly accommodative in recent years, including as a result of certain policies implemented by the Bank of England and HM Treasury such as the 'Funding for Lending' scheme, which have helped to support demand at a time of very pronounced fiscal tightening and balance sheet repair. There remains considerable uncertainty as to whether or when the Bank of England and other central banks will increase interest rates, following the US Federal Reserve's decision in December 2015 to raise US interest rates for the first time since 2006. A continued period of low interest rates and yield curves and spreads may affect the interest rate margin realised between lending and borrowing costs, the effect of which may be heightened during periods of liquidity stress.

Conversely, raising interest rates could lead to generally weaker than expected growth, or even contracting GDP, reduced business confidence, higher levels of unemployment or underemployment, adverse changes to levels of inflation, potentially higher interest rates and falling property prices in the markets in which the RBS Group operates, including the UK housing market, and consequently to an increase in delinquency rates and default rates among customers. Similar risks result from the exceptionally low level of inflation in developed economies, which in Europe particularly could deteriorate into sustained deflation if policy measures prove ineffective. Reduced monetary stimulus and the actions and commercial soundness of other financial institutions have the potential to impact market liquidity. Any adverse impact on the credit quality of the RBS Group's customers and other counterparties, coupled with a decline in collateral values, could lead to a reduction in recoverability and value of the RBS Group's assets and higher levels of impairment allowances, which could have an adverse effect on the RBS Group's and Group's operations, financial position or prospects. As part of ongoing derivatives operations, the RBS Group also faces significant basis, volatility and correlation risks, the occurrence of which are also impacted by the factors noted above.

Any such developments may also adversely impact the value of the RBS Group's pension fund which may result in additional contributions being required. See "*The RBS Group is subject to pension risks and may be required to make additional contributions to cover pension funding deficits and to restructure its pension schemes as a result of the implementation of the UK ring-fencing regime*."

Changes in currency rates, particularly in the sterling-US dollar and sterling-euro exchange rates, affect the value of assets, liabilities, income and expenses denominated in foreign currencies and the reported earnings of the RBS Group's non-UK subsidiaries and may affect the RBS Group's reported consolidated financial condition or its income from foreign exchange dealing. Such changes may result from the decisions of the ECB and of the US Federal Reserve and lead to sharp and sudden variations in foreign exchange rates, such as those seen in the GBP/USD exchange rates in 2015 and early 2016. For accounting purposes, the RBS Group carries some of its issued debt, such as debt securities, at the current market price on its balance sheet. Factors affecting the current market price for such debt, such as the credit spreads of the RBS Group, may result in a change to the fair value of such debt, which is recognised in the income statement as a profit or loss.

The performance and volatility of financial markets affect bond and equity prices and have caused, and may in the future cause, changes in the value of the RBS Group's investment and trading portfolios. Financial markets experienced significant volatility during 2015 and early 2016, following concerns about the political and economic recovery in Greece, volatility and instability in the Chinese and global stock markets and weakening fundamentals of the Chinese economy, resulting in further short-term changes in the valuation of certain of the RBS Group's assets. In addition, oil prices continued to fall significantly against their historical levels during 2015 and early 2016 and remained at such low levels, and other commodity prices also decreased.

Although it has significantly reduced its exposure in 2015, the RBS Group is exposed to oil and commodity prices though its exposure to customers and its other counterparties in the energy sector and oil producing countries. Further or sustained low oil and commodity prices could negatively impact the RBS Group's customers and other counterparties and the value of the RBS Group's trading portfolios.

The RBS Group's business performance and financial position could be adversely affected if its capital is not managed effectively or if it is unable to meet its capital targets.

Effective management of the RBS Group's capital is critical to its ability to operate its businesses, comply with its regulatory obligations, pursue its strategy of returning to stand-alone strength, resume dividend payments on its ordinary shares and maintain discretionary payments. The RBS Group is required by regulators in the UK, the EU and other jurisdictions in which it undertakes regulated activities to maintain adequate capital resources.

Adequate capital also gives the RBS Group financial flexibility in the face of continuing turbulence and uncertainty in the global economy and specifically in its core UK and European markets. On a fully loaded basis, the RBS Group's CET1 ratio was 15.5% at 31 December 2015.

During the restructuring period and until the implementation of the UK ring-fencing regime in 2019, the RBS Group has lifted its capital targets and currently aims to have a CET1 ratio at or over 13%. The RBS Group plans capital levels based on regulatory requirements and additional internal modelling and stress scenarios.

However, the RBS Group's ability to achieve such targets depends on a number of factors, including the implementation of its strategic programme and any of the factors described below. A shortage of capital could arise from:

- a depletion of the RBS Group's capital resources through increased costs or liabilities (including pension, conduct, litigation and legacy costs), reduced profits or losses (and therefore retained earnings) or reduced asset values resulting in write-downs or impairments;
- an increase in the amount of capital that is needed to be held, including as a result of changes to the actual level of risk faced by the RBS Group, changes in the minimum levels of capital or liquidity required by legislation or by the regulatory authorities or the calibration of capital or leverage buffers applicable to the RBS Group, including countercyclical buffers, increases in risk-weighted assets or in the risk weighting of existing asset classes or an increase in the RBS Group's view of the management buffer it should hold taking account of, for example, the capital levels or capital targets of the RBS Group's peer banks or through the changing views of rating agencies.

The RBS Group's current capital strategy is based on the expected accumulation of additional capital through the accrual of profit over time and/or through the planned reduction of its risk-weighted assets through disposals or natural attrition, the execution of which is subject to operational and market risks. Further losses or a failure to meet profitability targets or reduce risk-weighted assets in accordance with or within the timeline contemplated by the RBS Group's capital plan, combined with a depletion of its capital resources or an increase in the amount of capital it needs to hold (including as a result of the reasons described above), would adversely impact the RBS Group's ability to meet its capital targets or requirements and achieve its capital strategy during the restructuring period.

If circumstances were to result in the RBS Group having or being perceived to have a shortage of capital as a result of any of the circumstances described above, then it may be subject to regulatory interventions and sanctions and may suffer a loss of confidence in the market with the result that access to liquidity and funding may become constrained or more expensive. This may also trigger the implementation of its capital recovery plans.

This, in turn, may affect the RBS Group's capacity to continue its business operations, pay future dividends and make other distributions (including coupons on capital instruments) or pursue strategic opportunities, impacting future growth potential. If, in response to such shortage, the RBS Group is required to convert certain regulatory capital instruments into equity or raises additional capital through the issuance of share capital or regulatory capital instruments, existing RBSG shareholders may experience a dilution of their holdings. Separately, the RBS Group may address a shortage of capital by taking action to reduce leverage and/or risk-weighted assets, by modifying the RBS Group's legal entity structure or by asset or business disposals. Such actions may impact the underlying profitability of the RBS Group.

Failure by the RBS Group to comply with regulatory capital and leverage requirements may result in intervention by its regulators and loss of investor confidence, and may have a material adverse effect on its results of operations, financial condition and reputation and may result in distribution restrictions and adversely impact existing shareholders.

The RBS Group is subject to extensive regulatory supervision in relation to the levels and quality of capital in its business, including as a result of the transposition of the Basel Committee on Banking Supervision's regulatory capital framework ("Basel III") in Europe by a Directive and Regulation (collectively known as "CRD IV"). In addition, the RBS Group has been identified as a global systemically important bank ("GSIB") by the Financial Stability Board ("FSB") and is therefore subject to more intensive oversight and supervision by its regulators as well as additional capital requirements, although in the FSB's most recent annual list of GSIBs published in November 2015, the RBS Group was moved down to the last bucket, meaning that it will be subject to the lowest level of additional loss-absorbing capital requirements.

Under CRD IV, the RBS Group is required to hold at all times a minimum amount of regulatory capital calculated as a percentage of risk-weighted assets ("Pillar 1 requirement"). CRD IV also introduced six new capital buffers that are in addition to the Pillar 1 and Pillar 2A requirements (as described below) and are required to be met with CET1 capital. In December 2015, the Bank of England published a report on the framework of capital requirements for UK banks, which outlines the expectation that capital buffers be used actively by the regulator to serve a macro-prudential purpose. The combination of the capital conservation buffer (which, subject to transitional provisions, will be set at 2.5% from 2019), the countercyclical capital buffer (of up to 2.5%) and the higher of (depending on the institution) the systemic risk buffer, the global systemically important institutions buffer ("GSIB Buffer") and the other systemically important institutions buffer, is referred to as the "combined buffer requirement". These rules entered into force on 1 May 2014 for the countercyclical capital buffer and on 1 January 2016 for the capital conservation buffer and the GSIB buffer. The GSIB buffer is currently set at 1.5% for the RBS Group, but will reduce to 1.0% on 1 January 2017, and is being phased in over the period from 1 January 2017 to 1 January 2019.

The systemic risk buffer will be applicable from 1 January 2019. The Bank of England's Financial Policy Committee (the "FPC") is responsible for determining which institutions should hold the systemic risk buffer, and if so, how large the buffer should be up to a maximum of 3% of a firm's risk-weighted assets. The FPC is currently consulting on the proposed framework for the systemic risk buffer, with final rules to be finalised by 31 May 2016. The systemic risk buffer is part of the UK framework for identifying and setting higher capital buffers for domestic systemically important banks ("D-SIBs"), which are groups that, upon distress or failure, could have an important impact on their domestic financial systems.

This follows on 2012 framework recommendations by the FSB that national authorities should identify D-SIBs and take measures to reduce the probability and impact of the distress or failure of D-SIBs. In addition, national supervisory authorities may add extra capital requirements (the "Pillar 2A requirements") to cover risks that they believe are not covered or insufficiently covered by Pillar 1 requirements.

The RBS Group's current Pillar 2A requirement set by the PRA is set at an equivalent of 5.0% of risk-weighted assets. The PRA has also introduced a firm specific Pillar 2B buffer ("PRA buffer") which is a forward-looking requirement set annually and based on various factors including firm-specific stress test results and credible recovery and resolution planning and is to be met with CET1 capital (in addition to any CET1 capital used to meet any Pillar 1 or Pillar 2A requirements). Where appropriate, the PRA may require an increase in an institution's PRA Buffer to reflect additional capital required to be held to mitigate the risk of additional losses that could be incurred as a result of weak risk management and governance, including with respect to the effectiveness of the internal stress testing framework and control environment. UK banks are required to meet the higher of the combined buffer requirement or PRA buffer requirement. The Pillar 2A requirements and the PRA buffer will result in the setting of a fixed amount of CET1 capital which must be held by the RBS Group and which may change during the period of restructuring of the RBS Group, while risk-weighted assets are expected to continue to reduce during the same period, which will in turn put pressure on the RBS Group's ability to maintain its capital ratio targets and implement its distribution strategy.

In addition to capital requirements and buffers, the new regulatory framework adopted under CRD IV, as transposed in the UK, sets out minimum leverage ratio requirements for financial institutions. The FPC has directed the PRA to implement: (i) a minimum leverage requirement of 3% which applies to major UK banks, (ii) an additional leverage ratio to be met by GSIBs and ring-fenced institutions to be calibrated at 35% of the relevant firm's systemic risk capital buffer and which is being phased in from 2016 and (iii) a countercyclical leverage ratio buffer for all firms subject to the minimum leverage ratio requirements which is calibrated at 35% of a firm's countercyclical capital buffer.

Most of the capital requirements which apply or will apply to the RBS Group will need to be met in whole or in part with CET1 capital. CET1 capital broadly comprises retained earnings and equity instruments, including ordinary shares. As a result, the RBS Group may be required to issue additional ordinary shares in order to maintain or increase its CET1 capital if its retained earnings from the profits of its operations are insufficient, which could result in the dilution of existing shareholders.
Further, under the provisions of CRD IV Regulation, deferred tax assets that rely on future profitability (for example, deferred tax assets related to trade losses) and do not arise from temporary differences, must be deducted in full from CET1 capital. Other deferred tax assets which rely on future profitability and arise from temporary differences are subject to a threshold test and only the amount in excess of the threshold is deducted from CET1 capital. The regulatory treatment of such deferred tax assets may change and adversely impact the RBS Group's CET1 capital and related ratios.

The Basel Committee and other agencies remain focussed on changes that will increase, or recalibrate, measures of risk-weighted assets as the key measure of the different categories of risk in the denominator of the risk-based capital ratio. While they are at different stages of maturity, a number of initiatives across risk types and business lines are in progress that are expected to impact the calculation of risk-weighted assets. The Basel Committee is currently consulting on new rules relating to the risk weighting of real estate exposures and other changes to risk-weighting calculations. These rules are expected to be finalised later in 2016 and come into force by 2019. In the UK, the PRA is also considering ways of reducing the sensitivity of UK mortgage risk weights to economic conditions. The 2014 UK stress test demonstrated that the risk weights on some banks' residential mortgage portfolios can increase significantly in stressed conditions.

The Basel Committee also recently published for consultation a revised standardised measurement approach for operational risk. The new approach would replace the three existing standardised approaches for calculating operational risk, as well as the internal model-based approach. The proposed new methodology combines a financial statement-based measure of operational risk, with an individual firm's past operational losses. While the quantum of impact of these reforms remains uncertain owing to lack of clarity of the proposed changes and the timing of their introduction, the implementation of such initiatives could result in higher levels of risk-weighted assets and therefore higher levels of capital, and in particular CET1 capital, required to be held by the RBS Group, under Pillar 1 requirements. Such requirements would be separate from any further capital overlays required to be held as part of the PRA's determination of the RBS Group's Pillar 2A or PRA Buffer requirements with respect to such exposures.

If the RBS Group is unable to raise the requisite amount of regulatory capital, or to otherwise meet regulatory capital and leverage requirements, it may be exposed to increased regulatory supervision or sanctions, loss of investor confidence, restrictions on distributions and may be required to reduce further the amount of its risk-weighted assets or total assets and engage in the disposal of core and other non-core businesses, which may not occur on a timely basis or achieve prices which would otherwise be attractive to the RBS Group. A breach of the capital or leverage requirements applicable to the RBS Group or any relevant RBS Group entity, including the Group, may also trigger the application of the RBS Group's recovery plan to remediate a deficient capital position. A breach of the capital and leverage requirements applicable to the RBS Group may also result in the conversion into equity of certain regulatory capital instruments issued by the RBS Group or the issue of additional equity or regulatory capital instruments by the RBS Group, each of which could result in the dilution of the RBS Group's existing shareholders.

Failure by the RBS Group to comply with its capital requirements or to maintain sufficient distributable profits may result in the application of restrictions on its ability to make discretionary distributions, including the payment of dividends to its ordinary shareholders and coupons on certain capital instruments.

From 2016, in accordance with the provisions of CRD IV, a minimum level of capital adequacy is required to be met by the RBS Group in order for it to be entitled to make certain discretionary payments. Pursuant to Article 141 (Restrictions on distribution) of the CRD IV Directive, as transposed in the UK, institutions that fail to meet the "combined buffer requirement" will be subject to restricted "discretionary payments" (which are defined broadly by CRD IV as payments relating to CET1 (dividends), variable remuneration and coupon payments on additional Tier 1 instruments).

The restrictions are scaled according to the extent of the breach of the "combined buffer requirement" and calculated as a percentage of the profits of the institution since the last distribution of profits or "discretionary payment". The EBA has clarified that the CET1 capital to be taken into account for the MDA calculation should be limited to the amount not used to meet the Pillar 1 and Pillar 2 own funds requirements of the institution. In the event of a breach of the combined buffer requirement, the RBS Group will be required to calculate its MDA, and as a consequence it may be necessary for the RBS Group to reduce or cease discretionary payments to the extent of the breach. The ability of the RBS Group to meet the combined buffer requirement will be subject to the RBS Group holding sufficient CET1 capital in excess of its minimum Pillar 1 and Pillar 2 capital requirements. In addition, the interaction of such restrictions on distributions with the capital requirements and buffers applicable to the RBS Group remains uncertain in many respects while the relevant authorities in the EU and the UK consult on and develop their proposals and guidance on the application of the rules.

In addition, in order to make distributions (including dividend payments), the RBS Group is required to have sufficient distributable profits available. Furthermore, coupon payments due on the additional tier 1 instruments issued by the RBS Group must be cancelled in the event that the RBS Group has insufficient "distributable items" as defined under CRD IV. Both distributable profits and distributable items are largely impacted by the RBS Group's ability to generate and accumulate profits or conversely by material losses (including losses resulting from conduct related-costs, restructuring costs or impairments).

Failure by the RBS Group to meet the combined buffer requirement or retain sufficient distributable profits or distributable items as a result of reduced profitability or losses, or changes in regulation or taxes adversely impacting distributable profits or distributable items, may therefore result in limitations on the RBS Group's ability to make discretionary distributions which may negatively impact the RBS Group's shareholders, holders of additional tier 1 instruments, staff receiving variable compensation (such as bonuses) and other stakeholders and impact its market valuation and investors' and analysts' perception of its financial soundness.

The RBS Group is subject to stress tests mandated by its regulators in the UK and in Europe which may result in additional capital requirements which, in turn, may impact the RBS Group's financial condition, results of operations and investor confidence or result in restrictions on distributions.

The RBS Group is subject to stress tests by its regulator in the UK and by the European regulators with respect to RBS NV and Ulster Bank Ireland Limited. The results of the 2015 Bank of England stress tests showed that RBS's capital position remained above the Pillar 1 minimum capital requirements of 4.5% and met the leverage ratio of 3.0% in the hypothetical stress scenario. Although the PRA judged that the RBS Group did not meet its CET1 individual capital guidance after management actions in this scenario, in light of past and future plans to improve its capital position, the PRA did not require the RBS Group to submit a revised capital plan. In October 2015, the Bank of England published its approach to stress testing for the UK banking system applicable until 2018. The results of these tests will be used by the FPC and the PRA, alongside other inputs, to set the level of a financial institution's capital buffers, in particular the capital conservation buffer, countercyclical buffer and the PRA buffer.

The PRA will also use the stress test results to inform its determination of whether individual banks' current capital positions are adequate or need strengthening. For some banks, their individual stress-test results might imply that the capital conservation buffer and countercyclical rates set for all banks is not consistent with the impact of the stress on them. In that case, the PRA can increase regulatory capital buffers for individual banks by adjusting their PRA buffers. In addition, if the stress tests reveal that a bank's existing regulatory capital buffers are not sufficient to absorb the impact of the stress, it is possible that it will need to take action to strengthen its capital position. There is a strong presumption that the PRA would require a bank to take action if, at any point during the stress, a bank were projected to breach any of its minimum CET1 capital or leverage ratio requirements.

However, if a bank is projected to fail to meet its systemic buffers, it will still be expected to strengthen its capital position over time but the supervisory response is expected to be less intensive than if it were projected to breach its minimum capital requirements.

Failure by the RBS Group to meet the thresholds set as part of the stress tests carried out by its regulators in the UK and elsewhere may result in the RBS Group's regulators requiring the RBS Group to hold additional capital, increased supervision and/or regulatory sanctions, restrictions on capital distributions and loss of investor confidence, which may impact the RBS Group's and the Group's financial condition, results of operations and prospects.

As a result of extensive reforms being implemented within the EU and the UK relating to the resolution of financial institutions, additional requirements will arise to ensure that financial institutions maintain sufficient loss-absorbing capacity. Such changes to the funding and regulatory capital framework may require the RBS Group to meet higher funding levels than the RBS Group anticipated within its strategic plans and affect the RBS Group's funding costs.

In addition to the capital and leverage requirements under CRD IV, the EU Bank Recovery and Resolution Directive ("BRRD") introduces, among other things, a requirement for banks to maintain at all times a sufficient aggregate amount of own funds and "eligible liabilities" (that is, liabilities that can absorb loss and assist in recapitalising a firm in accordance with a predetermined resolution strategy), known as the minimum requirements for eligible liabilities ("MREL"), designed to ensure that the resolution of a financial institution may be carried out, without public funds being exposed to the risk of loss and in a way which ensures the continuity of critical economic functions, maintains financial stability and protects depositors. MREL is being implemented as part of the resolution planning process and not as a separate or additional capital requirement under Basel III. Indeed, if a bank's resolution plans are not deemed sufficient, the regulator can require it to carry higher MREL over and above regulatory minima and potentially higher than its peers. Certain capital resources required under CRD IV and associated institution-specific capital requirements set by the PRA or FCA may count toward meeting MREL, but the PRA has indicated its intention to prohibit certain double-counting of existing capital resources. In particular, CET1 capital used to meeting a financial institution's risk-weighted or leverage buffer requirements may not count towards meeting MREL requirements. As a result, the RBS Group may be required to issue additional instruments in the form of CET1 capital or subordinated or senior unsecured debt instruments and may result in an increased risk of a breach of the RBS Group's combined buffer requirement, triggering the restrictions relating to the MDA described above.

In addition to the requirements described above, the FSB published in November 2015 a final term sheet setting out its total loss-absorbing capacity ("TLAC") standards for global systemically important banks ("G-SIBs"). Although the Bank of England has indicated that it would use its powers to set MRELs for G-SIBs to implement the FSB's TLAC standards, the TLAC and MREL requirements differ in a number of ways.

The EBA is mandated to assess the implementation of MREL in the European Union and the consistency of MREL with the final TLAC standards in a report required by October 2016. This may result in the European Commission making amendments to the European regime on loss-absorbing requirements, which may in turn impact the UK authorities' implementation of the MREL requirements under the BRRD, and therefore may impact the quality or quantity of the capital required to be held by the RBS Group.

The UK government is required to transpose the BRRD's provisions relating to MREL into law through further secondary legislation with a requirement that the Bank of England take into account the final draft regulatory technical standards published by the EBA in July 2015. The Bank of England is responsible for setting the MREL requirements for each UK bank, building society and certain investment firms in consultation with the PRA and the FCA, and such requirement will be set depending on the resolution strategy of the financial institution. The Bank of England is currently consulting on the approach to be adopted in setting MREL, including, with respect to GSIBs, in line with the FSB's TLAC standards. GSIBs will be expected to meet their MREL requirements from 1 January 2019 and other financial institutions by 1 January 2020, subject to transitional arrangements. Until that time, MREL will be set equal to applicable minimum capital requirements, unless the Bank of England has particular concerns about a firm's resolvability. MREL requirements are expected to be set on a consolidated and individual basis, including for the holding entity of the banking group, at a level equivalent to two times the current minimum Pillar 1 and Pillar 2A capital requirements for that financial institution or, if higher, any applicable leverage ratio requirement, or the minimum capital requirements under Basel III plus, if applicable, capital buffer requirements: one for loss absorbency and one for recapitalisation.

For institutions, including the RBS Group, for which bail-in is the required resolution strategy and which are structured to permit single point of entry resolution due to their size and systemic importance, the Bank of England has indicated that in order to qualify as MREL, eligible liabilities (i.e. total loss-absorbing liabilities) will be expected to be issued from the resolution entity (i.e. the holding company for the RBS Group) and be structurally subordinated to operating and excluded liabilities (which include insured deposits, short-term debt, derivatives, structured notes and tax liabilities).

The capital raised through such issuances would then be transferred downstream to material operating subsidiaries (such as the Bank) in the form of capital or another form of subordinated claim. In this way, MREL resources will be structurally subordinated to senior liabilities of operating companies, allowing losses from operating companies to be transferred to the holding company and – if necessary – for resolution to occur at the holding company level, without placing the operating companies into a resolution process. In addition, the instruments which may qualify towards MREL will be determined in the PRA's final rules.

In order to achieve structural subordination for MREL purposes, senior unsecured issuances by RBSG will therefore need to be subordinated to the excluded liabilities described above. The TLAC standard includes an exemption from this requirement if the total amount of excluded liabilities on RBSG's balance sheet does not exceed 5% of its external TLAC (i.e. the eligible liabilities RBSG has issued to investors which meet the TLAC requirements) and the Bank of England has indicated in its consultation on MREL that it intends to adopt a similar approach.

Compliance with these and other future changes to capital adequacy and loss-absorbency requirements in the EU and the UK by the relevant deadline will require the RBS Group to restructure its balance sheet and issue additional capital compliant with the rules. In particular, these changes will require the RBS Group to issue Tier 1 capital (potentially including ordinary shares and additional Tier 1 instruments), Tier 2 capital and certain loss-absorbing debt securities, including senior securities, which may be costly and will result in certain existing Tier 1 and Tier 2 securities and other senior instruments issued by the RBS Group ceasing to count towards the RBS Group's loss-absorbing capital for the purposes of meeting MREL/TLAC requirements.

There remains considerable uncertainty as to how these rules will be implemented and the final requirements to which the RBS Group will be subject and the RBS Group may therefore need to revise its capital plan accordingly. The requirement to increase the RBS Group's levels of CET1 and Tier 2 capital, or other debt securities which qualify for meeting MREL, could have a number of negative consequences for the RBS Group and its shareholders, including impairing the RBS Group's potential future ability to pay dividends on, or make other distributions in respect of, ordinary shares and diluting the ownership of existing shareholders of RBSG.

The RBS Group's borrowing costs, its access to the debt capital markets and its liquidity depend significantly on its credit ratings and, to a lesser extent, on the rating of the UK Government.

The credit ratings of RBSG, the Bank and other RBS Group members directly affect the cost of, access to and sources of their financing and liquidity. A number of UK and other European financial institutions, including RBSG, the Bank and other RBS Group members, have been downgraded multiple times in recent years in connection with rating methodology changes and credit rating agencies' revised outlook relating to regulatory developments, macroeconomic trends and a financial institution's capital position and financial prospects.

During 2015, credit rating agencies completed their reviews and revisions of their ratings of banks by country to address the agencies' perception of the impact of ongoing regulatory changes designed to improve the resolvability of banks in a manner that minimises systemic risk, such that the likelihood of extraordinary support for failing banks is less predictable, as well as to address the finalisation of revised capital and leverage rules under CRD IV and firm-specific requirements.

As a result, RBSG's long-term and short-term credit ratings were downgraded by two notches by S&P and Fitch. S&P further downgraded the long-term credit rating of RBSG as a result of a number of factors, including S&P's assessment of the RBS Group's financial flexibility to absorb losses while a going concern, and the RBS Group's underperformance relative to similar peers in terms of profitability.

The long-term deposit and senior unsecured ratings for the Bank and certain other subsidiaries of RBSG, however, were upgraded by one notch to take into account the protection offered to senior unsecured creditors by loss-absorbing capital. Moody's also finalised its review of the RBS Group and downgraded RBSG's long-term senior unsecured and issuer credit ratings by two notches. As a result, the credit ratings of RBSG are below investment grade by that credit agency. The outlook for RBSG by Moody's is currently positive and is stable for S&P and Fitch.

Rating agencies regularly review the RBSG and RBS Group entity credit ratings, including those of the Bank, and their ratings of long-term debt are based on a number of factors, including the RBS Group's financial strength as well as factors not entirely within the RBS Group's control, including conditions affecting the financial services industry generally. In particular, the rating agencies may further review the ratings of RBSG, the Bank and other RBS Group entities as a result of the implementation of the UK ring-fencing regime, pension and litigation/regulatory investigation risk and other macroeconomic and political developments, including as a result of an outcome in favour of an exit from the European Union.

Any further reductions in the long-term or short-term credit ratings of RBSG, the Bank or of certain of its subsidiaries, including further downgrades below investment grade, could adversely affect the RBS Group's issuance capacity in the financial markets, increase its funding and borrowing costs, require RBS Group entities (including the Bank) to replace funding lost due to the downgrade, which may include the loss of customer deposits and may limit the RBS Group's access to capital and money markets and trigger additional collateral or other requirements in derivatives contracts and other secured funding arrangements or the need to amend such arrangements, limit the range of counterparties willing to enter into transactions with the RBS Group and its subsidiaries (including the Bank) and adversely affect its competitive position, all of which could have a material adverse impact on the RBS Group and the Group's earnings, cash flow and financial condition.

At 31 December 2015, a simultaneous one-notch long-term and associated short-term downgrade in the credit ratings of RBSG and the Bank by the three main ratings agencies would have required the RBS Group to post estimated additional collateral of £3.7 billion, without taking account of mitigating action by management. Individual credit ratings of RBSG, the Bank, The Royal Bank of Scotland N.V. ("RBS N.V.") and Ulster Bank Ireland Limited are also important to the RBS Group when competing in certain markets such as over-the-counter derivatives.

Any downgrade in the UK Government's credit ratings could also adversely affect the credit ratings of RBS Group companies (including the Bank) and may result in the effects noted above. In particular, political developments, including any exit, or uncertainty relating to a potential exit, of the UK from the European Union or the outcome of any further Scottish referendum could during a transitional period negatively impact the credit ratings of the UK Government and result in a downgrade of the credit ratings of RBSG, the Bank and RBS Group entities.

The RBS Group's ability to meet its obligations including its funding commitments depends on the RBS Group's ability to access sources of liquidity and funding.

Liquidity risk is the risk that a bank will be unable to meet its obligations, including funding commitments, as they fall due. This risk is inherent in banking operations and can be heightened by a number of factors, including an over-reliance on a particular source of wholesale funding (including, for example, short-term and overnight funding), changes in credit ratings or market-wide phenomena such as market dislocation and major disasters.

Credit markets worldwide, including interbank markets, have experienced severe reductions in liquidity and term funding during prolonged periods in recent years. In 2015, although the RBS Group's overall liquidity position remained strong, credit markets experienced increased volatility and certain European banks, in particular in the peripheral countries of Spain, Portugal, Greece and Italy, remained reliant on the ECB as one of their principal sources of liquidity.

The RBS Group relies on retail and wholesale deposits to meet a considerable portion of its funding. The level of deposits may fluctuate due to factors outside the RBS Group's control, such as a loss of confidence, increasing competitive pressures for retail customer deposits or the repatriation of deposits by foreign wholesale depositors, which could result in a significant outflow of deposits within a short period of time.

An inability to grow, or any material decrease in, the RBS Group's deposits could, particularly if accompanied by one of the other factors described above, have a material adverse impact on the RBS Group's ability to satisfy its liquidity needs. Increases in the cost of retail deposit funding may impact the RBS Group's margins and profitability.

The market view of bank credit risk has changed radically as a result of the financial crisis and banks perceived by the market to be riskier have had to issue debt at significantly higher costs. Although conditions have improved, there have been recent periods where corporate and financial institution counterparties have reduced their credit exposures to banks and other financial institutions, limiting the availability of these sources of funding.

The ability of the Bank of England to resolve the RBS Group in an orderly manner may also increase investors' perception of risk and hence affect the availability and cost of funding for the RBS Group. Any uncertainty relating to the credit risk of financial institutions may lead to reductions in levels of interbank lending or may restrict the RBS Group's access to traditional sources of funding or increase the costs or collateral requirements for accessing such funding.

The RBS Group has, at times, been required to rely on shorter-term and overnight funding with a consequent reduction in overall liquidity, and to increase its recourse to liquidity schemes provided by central banks. Such schemes require assets to be pledged as collateral. Changes in asset values or eligibility criteria can reduce available assets and consequently available liquidity, particularly during periods of stress when access to the schemes may be needed most. The implementation of the UK ring-fencing regime may also impact the RBS Group's funding strategy and the cost of funding may increase for certain Group entities, including the Bank, which may be required to manage their own funding and liquidity strategy, in particular those entities outside the ring-fence which will no longer be able to rely on retail deposit funding.

If the RBS Group is unable to raise funds through deposits and/or in the capital markets, its liquidity position could be adversely affected and it might be unable to meet deposit withdrawals on demand or at their contractual maturity, to repay borrowings as they mature, to meet its obligations under committed financing facilities, to comply with regulatory funding requirements or to fund new loans, investments and businesses. The RBS Group may need to liquidate unencumbered assets to meet its liabilities, including disposals of assets not previously identified for disposal to reduce its funding commitments. In a time of reduced liquidity, the RBS Group may be unable to sell some of its assets, or may need to sell assets at depressed prices, which in either case could have a material adverse effect on the RBS Group's and the Group's financial condition and results of operations.

The RBS Group's businesses are subject to substantial regulation and oversight. Significant regulatory developments and increased scrutiny by the RBS Group's key regulators has had and is likely to continue to increase compliance and conduct risks and could have a material adverse effect on how the RBS Group conducts its business and on its results of operations and financial condition.

The RBS Group is subject to extensive financial services laws, regulations, corporate governance requirements, administrative actions and policies in each jurisdiction in which it operates. Many of these have been introduced or amended recently and are subject to further material changes. Among others, the adoption of rules relating to the UK ring-fencing regime, prohibitions on proprietary trading, the entry into force of CRD IV and the BRRD and certain other measures in the UK, the EU and the US are considerably affecting the regulatory landscape in which the RBS Group and the Group operate and will operate in the future.

Increased regulatory focus in certain areas, including conduct, consumer protection regimes, anti-money laundering and antiterrorism laws and regulations, as well as the provisions of applicable sanctions programmes and ongoing and possible future changes in the financial services regulatory landscape (including requirements imposed by virtue of the RBS Group's participation in government or regulator-led initiatives), have resulted in the RBS Group facing greater regulation and scrutiny in the UK, the US and other countries in which it operates.

Although it is difficult to predict with certainty the effect that the recent regulatory changes, developments and heightened levels of public and regulatory scrutiny will have on the RBS Group, including the Bank, the enactment and implementation of legislation and regulations in the UK and the EU, the other parts of Europe in which the RBS Group operates and the US has resulted in increased capital, funding and liquidity requirements, changes in the competitive landscape, changes in other regulatory requirements and increased operating costs, and has impacted, and will continue to impact, product offerings and business models. Such changes may also result in an increased number of regulatory investigations and proceedings and have increased the risks relating to the RBS Group's ability to comply with the applicable body of rules and regulations in the manner and within the time frames required. Changes in accounting standards or guidance by internal accounting bodies or in the timing of their implementation, whether mandatory or as a result of recommended disclosure relating to the future implementation of such standards could also result in the RBS Group having to recognise additional liabilities on its balance sheet, or in further write-downs or impairments. Any of these developments (including failures to comply with new rules and regulations) could have an impact on how the RBS Group conducts its business, its authorisations and licences, the products and services it offers, its reputation and the value of its assets, and could have a material adverse effect on the RBS Group's and/or the Group's business, funding costs and results of operations and financial condition.

Areas in which, and examples of where, governmental policies, regulatory and accounting changes and increased public and regulatory scrutiny could have an adverse impact (some of which could be material) on the RBS Group include those set out above as well as the following:

- amendments to the framework or requirements relating to the quality and quantity of regulatory capital to be held by the RBS Group or the Group, either on a solo, consolidated or sub-group level, including amendments to the rules relating to the calculation of risk-weighted assets and reliance on credit ratings as well as tax rules affecting the eligibility of deferred tax assets;
- new or amended regulations or taxes that reduce profits attributable to shareholders which may diminish, or restrict, the accumulation of the distributable profits or distributable items necessary to make distributions or coupon payments;
- the design and implementation of national or supranational mandated recovery, resolution or insolvency regimes or the implementation of additional or conflicting loss-absorption requirements, including those mandated under MREL or by the Financial Stability Board's recommendations on TLAC;
- the monetary, fiscal, interest rate and other policies of central banks and other governmental or regulatory bodies;
- further investigations, proceedings or fines either against the RBS Group in isolation or together with other large financial institutions with respect to market conduct wrongdoing;
- the imposition of government-imposed requirements and/or related fines and sanctions with respect to lending to the UK SME market and larger commercial and corporate entities and residential mortgage lending; additional rules and regulatory initiatives and review relating to customer protection, including the FCA's Treating Customers Fairly regime and increased focus by regulators on how institutions conduct business, particularly with regard to the delivery of fair outcomes for customers and orderly/transparent markets;
- the imposition of additional restrictions on the RBS Group's ability to compensate its senior management and other employees and increased responsibility and liability rules applicable to senior and key employees;
- regulations relating to, and enforcement of, anti-bribery, anti-money laundering, anti-terrorism or other similar sanctions regimes;
- rules relating to foreign ownership, expropriation, nationalisation and confiscation of assets;
- changes to financial reporting standards (including accounting standards) and guidance or the timing of their implementation;
- changes to risk aggregation and reporting standards;
- changes to corporate governance requirements, corporate structures and conduct of business rules;
- competition reviews and investigations relating to the retail banking sector in the UK, including with respect to SME banking and PCAs;
- financial market infrastructure reforms in the EU establishing new rules applying to investment services, short selling, market abuse and investment funds;
- increased attention to competition and innovation in UK payment systems following the establishment of the new Payments Systems Regulator and developments relating to current European proposals for a directive on payment services;
- restrictions on proprietary trading and similar activities within a commercial bank and/or a group;
- the introduction of, and changes to, taxes, levies or fees applicable to the RBS Group's operations, such as the imposition of a financial transaction tax, changes in tax rates, the introduction of the bank corporation surcharge of 8% which came into effect on 1 January 2016 or changes to the treatment of carry-forward tax losses that reduce the value of deferred tax assets and require increased payments of tax;
- investigations into facilitation of tax evasion or the creation of new civil or criminal offences relating thereto;
- the regulation or endorsement of credit ratings used in the EU (whether issued by agencies in EU member states or in other countries, such as the US); and
- other requirements or policies affecting the RBS Group's profitability, such as the imposition of onerous compliance obligations, further restrictions on business growth, product offering, or pricing.

Changes in laws, rules or regulations, or in their interpretation or enforcement, or the implementation of new laws, rules or regulations, including contradictory laws, rules or regulations by key regulators in different jurisdictions, or failure by the RBS Group to comply with such laws, rules and regulations, may have a material adverse effect on the RBS Group's and/or the Group's business, financial condition and results of operations. In addition, uncertainty and lack of international regulatory coordination as enhanced supervisory standards are developed and implemented may adversely affect the RBS Group's ability to engage in effective business, capital and risk management planning.

The RBS Group is currently implementing a number of significant investment and rationalisation initiatives as part of the RBS Group's IT investment programme. Should such investment and rationalisation initiatives fail to achieve the expected results, it could have a material adverse impact on the RBS Group's operations and its ability to retain or grow its customer business and could require the RBS Group to recognise impairment charges.

The RBS Group's strategic programme to simplify and downsize the RBS Group with an increased focus on service to its customers involves significant investments in technology and more efficient support functions intended to contribute to delivering significant improvements in the RBS Group's Return on Equity and cost–to-income ratio in the longer term as well as improve the resilience, control environment, accessibility and product offering of the RBS Group. The RBS Group has an IT transformational budget of around £4 billion (which excludes IT expenditure and costs relating to the implementation of the UK ring-fencing regime and the Williams & Glyn separation) to be spent from 2015 to 2017. At 31 December 2015, £1.2 billion of this budget had already been spent, and the budget for 2016 and 2017 is now higher than previously estimated as business plans have developed.

This investment in the RBS Group's IT capability will be used to further simplify and upgrade its IT systems and capabilities to make them more cost-effective and improve controls and procedures, enhance the digital services provided to its bank customers and address system failures which adversely affect its relationship with its customers and reputation and may lead to regulatory investigations and redress.

As with any project of comparable size and complexity, there can be no assurance that the RBS Group will be able to implement all of the initiatives forming part of its IT investment programme, on time or at all, and it may experience unexpected cost increases and delays. This is especially true in light of the separation of the Williams & Glyn business which requires the delivery of a stand-alone IT platform for the separated business, and the focus on meeting this requirement may limit the RBS Group's capacity and resources to implement the planned changes to the RBS Group IT infrastructure while the separation work is ongoing. Any failure by the RBS Group to realise the benefits of its IT investment programme, whether on time or at all, could have a material adverse effect on the RBS Group's and/or the Group's business, results of operations and its ability to retain or grow its customer business.

The RBS Group's operations are highly dependent on its IT systems. A failure of the RBS Group's IT systems could adversely affect its operations and investor and customer confidence and expose the RBS Group to regulatory sanctions.

The RBS Group's operations are dependent on the ability to process a very large number of transactions efficiently and accurately while complying with applicable laws and regulations where it does business. The proper functioning of the RBS Group's payment systems, financial and sanctions controls, risk management, credit analysis and reporting, accounting, customer service and other IT systems, as well as the communication networks between its branches and main data processing centers, are critical to the RBS Group's operations.

The vulnerabilities of the RBS Group's IT systems are due to their complexity, attributable in part to overlapping multiple legacy systems resulting from the RBS Group's historical acquisitions and insufficient investment prior to 2013, creating challenges in recovering from system breakdowns.

IT failures adversely affect the RBS Group's relationship with its customers and reputation and have led, and may in the future, lead to regulatory investigations and redress. The RBS Group experienced system failures in 2012, as a result of which the RBS Group was required to set aside a provision for compensation to customers who suffered losses as a result of the system failure and that resulted in the RBS Group reaching a settlement with the FCA, the PRA and the Central Bank of Ireland and paying related fines. The RBS Group experienced a limited number of IT failures in 2015 affecting customers, although improvements introduced since 2012 allowed the RBS Group to contain the impact of such failures.

The RBS Group's regulators in the UK are actively surveying progress made by banks in the UK to modernise, manage and secure their IT infrastructures, in order to prevent future failures affecting customers. Any critical system failure, any prolonged loss of service availability or any material breach of data security could cause serious damage to the RBS Group's ability to service its customers, could result in significant compensation costs or fines resulting from regulatory investigations and could breach regulations under which the RBS Group operates. In particular, failures or breaches resulting in the loss or publication of confidential customer data could cause long-term damage to the RBS Group's and/or the Group's reputation, business and brands, which could undermine its ability to attract and keep customers.

The RBS Group is currently implementing a number of complex initiatives, including its strategic programme, the UK ring-fencing regime, the separation of the Williams & Glyn business, the restructuring of the CIB business and a significant IT investment programme, all which may put further strains on the RBS Group's existing IT systems. A failure to safely and timely implement one or several of these initiatives could lead to disruptions of the RBS Group's IT infrastructure and in turn cause long-term damage to the RBS Group's and/or the Group's reputation, brands, results of operations and financial position. See *"The RBS Group is currently implementing a number of significant investment and rationalisation initiatives as part of the RBS Group's IT investment programme. Should such investment and rationalisation initiatives fail to achieve the expected results, it could have a material adverse impact on the RBS Group's operations and its ability to retain or grow its customer business and could require the RBS Group to recognise impairment charges."*

The RBS Group is exposed to cyberattacks and a failure to prevent or defend against such attacks could have a material adverse effect on the RBS Group's and the Group's operations, results of operations or reputation.

The RBS Group is subject to cybersecurity threats which have regularly targeted financial institutions as well as governments and other institutions and have increased in frequency and severity in recent years. The RBS Group relies on the effectiveness of its internal policies and associated procedures, infrastructure and capabilities to protect the confidentiality, integrity and availability of information held on its computer systems, networks and mobile devices, and on the computer systems, networks and mobile devices of third parties on whom the RBS Group relies.

The RBS Group also takes measures to protect itself from attacks designed to prevent the delivery of critical business processes to its customers. Despite these preventative measures, the RBS Group's computer systems, software, networks and mobile devices, and those of third parties on whom the RBS Group relies, are vulnerable to cyberattacks, sabotage, unauthorised access, computer viruses, worms or other malicious code, and other events that have a security impact.

Failure to protect the RBS Group's operations from cyberattacks or to continuously review and update current processes in response to new threats could result in the loss of customer data or other sensitive information as well as instances of denial of service for the RBS Group's customers. During 2015, the RBS Group experienced a number of distributed denial of service ("DDoS") attacks, one of which had a temporary impact on some of NatWest's web services, as well as a smaller number of malware attacks. The Bank of England, the FCA and HM Treasury in the UK and regulators, in the US and in Europe have identified cybersecurity as a systemic risk to the financial sector and highlighted the need for financial institutions to improve resilience to cyberattacks and the RBS Group expects greater regulatory engagement, supervision and enforcement on cybersecurity in the future. The RBS Group participated in the Bank of England's industry-wide exercise in 2015 to test how a major firm responds to significant cyberattacks against its critical economic functions.

The outputs of this exercise and other regulatory and industry-led initiatives are being incorporated into the RBS Group's on-going IT priorities and improvement measures. The RBS Group expects to be the target of continued attacks in the future and there can be no assurance that the RBS Group will be able to prevent all threats. Any failure in the RBS Group's cybersecurity policies, procedures or capabilities, or cyber-related crime, could lead to the RBS Group suffering reputational damage and a loss of customers, regulatory investigations or sanctions being imposed and could have a material adverse effect on the RBS Group's and/or the Group's results of operations, financial condition or prospects.

The RBS Group's operations entail inherent reputational risk.

Reputational risk, meaning the risk of brand damage and/or financial loss due to a failure to meet stakeholders' expectations of the RBS Group's conduct, performance and business profile, is inherent in the RBS Group's business. Stakeholders include customers, investors, rating agencies, employees, suppliers, governments, politicians, regulators, special interest groups, consumer groups, media and the general public.

Brand damage can be detrimental to the business of the RBS Group in a number of ways, including its ability to build or sustain business relationships with customers, low staff morale, regulatory censure or reduced access to, or an increase in the cost of, funding. In particular, negative public opinion resulting from the actual or perceived manner in which the RBS Group conducts its business activities and operations, the RBS Group's financial performance, ongoing investigations and proceedings and the settlement of any such investigations and proceedings, IT failures or cyber-attacks resulting in the loss or publication of confidential customer data or other sensitive information, the level of direct and indirect government support, or actual or perceived practices in the banking and financial industry may adversely affect the RBS Group's ability to keep and attract customers and, in particular, corporate and retail depositors.

Modern technologies, in particular online social networks and other broadcast tools which facilitate communication with large audiences in short time frames and with minimal costs, may also significantly enhance and accelerate the impact of damaging information and allegations. Reputational risks may also be increased as a result of the restructuring of the RBS Group to implement its strategic programme and the UK ring-fencing regime. Although the RBS Group has implemented a Reputational Risk Policy across customer-facing businesses to improve the identification, assessment and management of customers, transactions, products and issues which represent a reputational risk, the RBS Group cannot ensure that it will be successful in avoiding damage to its business from reputational risk, which could result in a material adverse effect on the RBS Group's and/or the Group's business, financial condition, results of operations and prospects.

The RBS Group is exposed to conduct risk which may adversely impact the RBS Group or its employees and may result in conduct having a detrimental impact on the RBS Group's customers or counterparties.

In recent years, the RBS Group has sought to refocus its culture on serving the needs of its customers and continues to redesign many of its systems and processes to promote this focus and strategy. However, the RBS Group is exposed to various forms of conduct risk in its operations. These include business and strategic planning that does not consider customers' needs, ineffective management and monitoring of products and their distribution, a culture that is not customer-centric, outsourcing of customer service and product delivery via third parties that do not have appropriate levels of control, oversight and culture, the possibility of alleged mis-selling of financial products or the mishandling of complaints related to the sale of such product, or poor governance of incentives and rewards. Some of these risks have materialised in the past and ineffective management and oversight of conduct issues may result in customers being poorly or unfairly treated and may in the future lead to further remediation and regulatory intervention/enforcement.

The RBS Group's businesses are also exposed to risk from employee misconduct including non-compliance with policies and regulatory rules, negligence or fraud, any of which could result in regulatory sanctions and serious reputational or financial harm to the RBS Group. In recent years, a number of multinational financial institutions, including the RBS Group, have suffered material losses due to the actions of employees, including, for example, in connection with the foreign exchange and LIBOR investigations. It is not always possible to deter employee misconduct and the precautions the RBS Group takes to prevent and detect this activity may not always be effective.

The RBS Group has implemented a number of policies and allocated new resources in order to help mitigate against these risks. The RBS Group has also prioritised initiatives to reinforce good conduct in its engagement with the markets in which it operates, together with the development of preventative and detective controls in order to positively influence behaviour.

The RBS Group's strategic programme is also intended to improve the RBS Group's control environment. Nonetheless, no assurance can be given that the RBS Group's strategy and control framework will be effective and that conduct issues will not have an adverse effect on the RBS Group's and/or the Group's results of operations, financial condition or prospects.

The RBS Group and the Group may be adversely impacted if the RBS Group's risk management is not effective.

The management of risk is an integral part of all of the RBS Group's activities. Risk management comprises the definition and monitoring of the RBS Group's risk appetite and reporting of the RBS Group's exposure to uncertainty and the consequent adverse effect on profitability or financial condition arising from different sources of uncertainty and risks as described throughout these risk factors. Ineffective risk management may arise from a wide variety of events and behaviours, including lack of transparency or incomplete risk reporting, unidentified conflicts or misaligned incentives, lack of accountability control and governance, lack of consistency in risk monitoring and management or insufficient challenges or assurance processes.

Failure to manage risks effectively could adversely impact the RBS Group's reputation or its relationship with its customers, shareholders or other stakeholders, which in turn could have a significant effect on the RBS Group's and/or the Group's business prospects, financial condition and/or results of operations.

Risk management is also strongly related to the use and effectiveness of internal stress tests and models. See *"The RBS Group relies on valuation, capital and stress test models to conduct its business, assess its risk exposure and anticipate capital and funding requirements. Failure of these models to provide accurate results or accurately reflect changes in the micro and macroeconomic environment in which the RBS Group operates could have a material adverse effect on the RBS Group's and/or the Group's business, capital and results."*

A failure by the RBS Group to embed a strong risk culture across the organisation could adversely affect the RBS Group's ability to achieve its strategic objective.

In response to weaknesses identified in previous years, the RBS Group is currently seeking to embed a strong risk culture within the organisation based on a robust risk appetite and governance framework. A key component of this approach is the three lines of defence model designed to identify, manage and mitigate risk across all levels of the organisation. This framework is still in the process of being implemented and improvements continue and will continue to be made to clarify and improve the three lines of defence and internal risk responsibilities and resources, including in response to feedback from regulators. A failure by any of these three lines to carry out their responsibilities or to effectively embed this culture could have a material adverse effect on the RBS Group through an inability to achieve its strategic objectives for its customers, employees and wider stakeholders.

The RBS Group is subject to pension risks and may be required to make additional contributions to cover pension funding deficits and to restructure its pension schemes as a result of the implementation of the UK ring-fencing regime.

The RBS Group maintains a number of defined benefit pension schemes for certain former and current employees. Pension risk is the risk that the assets of the RBS Group's various defined benefit pension schemes do not fully match the timing and amount of the schemes' liabilities, as a result of which the RBS Group is required or chooses to make additional contributions to address deficits that may emerge. Risk arises from the schemes because the value of the asset portfolios may be less than expected and because there may be greater than expected increases in the estimated value of the schemes' liabilities and additional future contributions to the schemes may be required.

The value of pension scheme liabilities varies with changes to long-term interest rates (including prolonged periods of low interest rates as is currently the case), inflation, monetary policy, pensionable salaries and the longevity of scheme members, as well as changes in applicable legislation. In particular, as life expectancies increase, so too will the pension scheme liabilities; as the impact on the pension scheme liabilities due to a one year increase in longevity is expected to be £853 million. In addition, as the RBS Group expects to continue to materially reduce the scope of its operations as part of the implementation of its strategic programme and of the UK ring-fencing regime, pension liabilities will therefore increase relative to the size of the RBS Group, which may impact the RBS Group's results of operations and capital position.

Given recent economic and financial market difficulties and volatility, the low interest rate environment and the risk that such conditions may occur again over the near and medium term, the RBS Group has experienced increasing pension deficits and was required to make further contributions following the last triennial valuation of The Royal Bank of Scotland Group Pension Fund, the RBS Group's main defined benefit pension scheme (the "Main Scheme"), which showed that the value of liabilities exceeded the value of assets by £5.6 billion at 31 March 2013, a ratio of 82%. Following the publication of the IASB's exposure draft of amendments to IFRIC 14, the RBS Group has revised its pension accounting policy for determining whether or not it has an unconditional right to a refund of any surpluses in its employee pension funds. This change has resulted in the accelerated recognition of a £4.2 billion liability corresponding to the nominal value of all committed contributions in respect of past service pursuant to the May 2014 triennial valuation agreement with the Main Scheme pension trustee.

The RBS Group has agreed in principle with the Main Scheme pension trustee to make an accelerated cash payment of the outstanding committed future contributions (£4.2 billion) to the Main Scheme (the majority of which payment has been provided for as a result of the accounting policy change described above) and to bring forward the next triennial valuation to be as of a date between 31 October 2015 and 31 December 2015.

The contribution of £4.2 billion was paid in March 2016. The 2015 triennial valuation is expected to result in a significant increase in the regular annual contributions in respect of the ongoing accrual of benefits. This will have the effect of significantly decreasing the amount of any pension surplus that the RBS Group can recognise as a balance sheet asset.

The next triennial period valuation will therefore take place in Q4 2018 and the Main Scheme pension trustee has agreed that it would not seek a new valuation prior to that date, except where a material change arises. Notwithstanding this accelerated payment and any additional contributions which may be required beforehand as a result of a material change, the RBS Group expects to have to agree to additional contributions, over and above the existing committed past service contributions, from Q1 2020 as a result of the next triennial valuation. The underlying assumptions used to calculate the triennial valuation deficit as at 31 March 2013 are set out further in note 4 Pensions on page 168.

The cost of such additional contributions could be material and any additional contributions that are committed to the Main Scheme following new actuarial valuations would in turn, under RBS's revised accounting policy, trigger the recognition of a significant additional liability in the RBS Group's accounts, which in turn could have a material adverse effect on the RBS Group's and/or the Group's results of operations, financial position and prospects.

In addition, the UK ring-fencing regime will require significant changes to the structure of the RBS Group's existing defined benefit pension schemes as RFB entities may not be liable for debts to pension schemes that might arise as a result of the failure of another entity of the ring-fenced bank's group after 1 January 2026. The restructuring of the RBS Group's defined benefit pension plans to implement the UK ring-fencing regime, could affect assessments of the RBS Group's pension scheme deficits, or result in the pension scheme trustees making a determination that the employer covenant has been weakened, and result in additional contributions being required.

The RBS Group is developing a strategy to meet these requirements, which has been discussed with the PRA and will require the agreement of the pension scheme trustee. Discussions with the pension scheme trustee will be influenced by the RBS Group's overall ring-fence strategy and its pension funding and investment strategies. If agreement is not reached with the pension trustee, alternative options less favourable to the RBS Group will need to be developed to meet the requirements of the pension regulations.

The costs associated with the restructuring of the RBS Group's existing defined benefit pension schemes could be material and could result in higher levels of additional contributions than those described above and currently agreed with the pension trustee which could have a material adverse effect on the RBS Group's and/or the Group's results of operations, financial position and prospects.

Pension risk and changes to the RBS Group's funding of its pension schemes may have a significant impact on the RBS Group's capital position.

The RBS Group's capital position is influenced by pension risk in several respects: Pillar 1 capital is impacted by the requirement that net asset pension balances are to be deduced from capital and that actuarial gains/losses impact reserves and, by extension, CET1 capital; Pillar 2A requirements result in the RBS Group being required to carry a capital add-on to mitigate stress on the pension fund and finally the RBS Group's target CET1 ratio incorporates a management buffer over the combined buffer requirement which assumes, amongst other risks, a buffer to mitigate a deterioration in the RBS Group's pension fund position.

The RBS Group believes that the accelerated payment to the RBS Group's Main Scheme pension fund will improve the RBS Group's capital planning and resilience through the period to 2019 and provide the Main Scheme pension trustee with more flexibility over its investment strategy.

The RBS Group estimates that the accelerated payment will adversely impact the RBS Group's CET1 capital in 2016 by 30 to 40 basis points and reduce the RBS Group's MDA level of CET1 capital or management buffer capital required for pension risk which may trigger MDA requirements and result in mandatory restrictions on discretionary distributions. The RBS Group's expectations as to the impact on its capital position of this payment in the near and medium term and of the accounting impact under its revised accounting policy are based on a number of assumptions and estimates, including with respect to the beneficial impact on its Pillar 2A requirements and confirmation of such impact by the PRA and the timing thereof, any of which may prove to be inaccurate (including with respect to the calculation of the CET1 ratio impact on future periods), including as a result of factors outside of the RBS Group's control (which include the PRA's approval).

As a result, if any of these assumptions proves inaccurate, the RBS Group's capital position may significantly deteriorate and fall below the RBS Group's or RBS Group entities (including the Bank's) minimum capital requirements and in turn result in increased regulatory supervision or sanctions, restrictions on discretionary distributions or loss of investor confidence, which could individually or in aggregate have a material adverse effect on the RBS Group's and/or the Group's results of operations, financial prospects or reputation.

The impact of the RBS Group's pension obligations on its results and operations are also dependent on the regulatory environment in which it operates.

There is a risk that changes in prudential regulation, pension regulation and accounting standards, or a lack of coordination between such sets of rules, may make it more challenging for the RBS Group to manage its pension obligations resulting in an adverse impact on the RBS Group's CET1 capital.

The RBS Group's business and results of operations may be adversely affected by increasing competitive pressures and technology disruption in the markets in which it operates.

The markets for UK financial services, and the other markets within which the RBS Group operates, are very competitive, and management expects such competition to continue or intensify in response to customer behaviour, technological changes (including the growth of digital banking), competitor behaviour, new entrants to the market (including non traditional financial services providers such as large retail or technology conglomerates), new lending models (such as peer-to-peer lending) and the impact of regulatory actions and other factors. In particular, the emergence of disintermediation in the financial sector resulting from new banking, lending and payment solutions offered by rapidly evolving incumbents, challengers and new entrants, in particular with respect to payment services and products, and the introduction of disruptive technology may impede the RBS Group's ability to grow or retain its market share and impact its revenues and profitability, particularly in its key UK retail banking segment. Increasingly many of the products and services offered by the RBS Group are, and will become, technology intensive and the RBS Group's ability to develop such services has become increasingly important to retaining and growing the RBS Group's customer business in the UK.

There can be no certainty that the RBS Group's investment in its IT capability intended to address the material increase in customer use of online and mobile technology for banking will be successful or that it will allow the RBS Group to continue to grow such services in the future. Certain of the RBS Group's current or future competitors may have more efficient operations, including better IT systems allowing them to implement innovative technologies for delivering services to their customers. Furthermore, the RBS Group's competitors may be better able to attract and retain customers and key employees and may have access to lower cost funding and/or be able to attract deposits on more favourable terms than the RBS Group. If the RBS Group is unable to offer competitive, attractive and innovative products that are also profitable, it could lose market share, incur losses on some or all of its activities and lose opportunities for growth.

In addition, recent and future disposals and restructurings by the RBS Group relating to the implementation of its strategic programme and the UK ring-fencing regime, or required by the RBS Group's regulators, as well as constraints imposed on the RBS Group's ability to compensate its employees at the same level as its competitors, may also have an impact on its ability to compete effectively.

Intensified competition from incumbents, challengers and new entrants in the RBS Group's core markets could lead to greater pressure on the RBS Group to maintain returns and may lead to unsustainable growth decisions.

These and other changes in the RBS Group's competitive environment could have a material adverse effect on the RBS Group's and/or the Group's business, margins, profitability, financial condition and prospects.

The RBS Group operates in markets that are subject to intense scrutiny by the competition authorities and its business and results of operations could be materially affected by competition rulings and other government measures.

The competitive landscape for banks and other financial institutions in the UK, the rest of Europe and the US is changing rapidly. Recent regulatory and legal changes have and may continue to result in new market participants and changed competitive dynamics in certain key areas, such as in retail banking in the UK where the introduction of new entrants is being actively encouraged by the UK Government. The competitive landscape in the UK is also likely to be affected by the UK Government's implementation of the UK ring-fencing regime and other customer protection measures introduced by the Banking Reform Act 2013. The implementation of these reforms may result in the consolidation of newly separated businesses or assets of certain financial institutions with those of other parties to realise new synergies or protect their competitive position and is likely to increase competitive pressures on the RBS Group.

The UK retail banking sector has been subjected to intense scrutiny by the UK competition authorities and by other bodies in recent years, including market reviews conducted by the Competition & Markets Authority ("CMA") and its predecessor the Office of Fair Trading regarding SME banking and Personal Current Accounts ("PCAs"), the Independent Commission on Banking and the Parliamentary Commission on Banking Standards. These reviews raised significant concerns about the effectiveness of competition in the banking sector.

Although these reviews are ongoing, preliminary findings in the CMA's Retail Banking Market Investigation contemplated proposing measures primarily intended to make it easier for consumers and businesses to compare bank products and increase the transparency of price comparison between banks and amend overdraft charging, which would, if implemented, impose additional compliance requirements on the RBS Group and could, in aggregate, adversely impact the RBS Group's competitive position, product offering and revenues. The wholesale banking sector has also been the subject of recent scrutiny. In February 2015 the FCA announced that it would be launching a market study to investigate competition in investment and corporate banking services. The FCA is expected to publish its interim report in early 2016 and its final report in spring 2016.

Adverse findings resulting from current or future competition investigations may result in the imposition of reforms or remedies which may impact the competitive landscape in which the RBS Group operates or result in restrictions on mergers and consolidations within the UK financial sector.

The impact of any such developments in the UK will become more significant as the RBS Group's business becomes increasingly concentrated in the UK retail sector. These and other changes to the competitive framework in which the RBS Group operates could have a material adverse effect on the RBS Group's and/or the Group's business, margins, profitability, financial condition and prospects.

As a result of the commercial and regulatory environment in which it operates, the RBS Group may be unable to attract or retain senior management (including members of the board) and other skilled personnel of the appropriate qualification and competence. The RBS Group may also suffer if it does not maintain good employee relations.

Implementation of the RBS Group's strategic programme and its future success depend on its ability to attract, retain and remunerate highly skilled and qualified personnel, including senior management (which includes directors and other key employees), in a highly competitive labour market. This cannot be guaranteed, particularly in light of heightened regulatory oversight of banks and the increasing scrutiny of, and (in some cases) restrictions placed upon, employee compensation arrangements, in particular those of banks in receipt of Government support (such as the RBS Group), which may place the RBS Group at a competitive disadvantage. In addition, the market for skilled personnel is increasingly competitive, thereby raising the cost of hiring, training and retaining skilled personnel.

Certain of the RBS Group's directors as well as members of its executive committee and certain other senior managers and employees will also be subject to the new responsibility regime introduced under the Banking Reform Act 2013 which introduces clearer accountability rules for those within the new regime. The senior managers' regime and certification regime take effect on 7 March 2016, whilst the conduct rules will apply to the wider employee population from 7 March 2017 onwards, with the exception of some transitional provisions. The new regulatory regime may contribute to reduce the pool of candidates for key management and non-executive roles, including non-executive directors with the right skills, knowledge and experience, or increase the number of departures of existing employees, given concerns over the allocation of responsibilities introduced by the new rules.

The RBS Group's evolving strategy has led to the departure of a large number of experienced and capable employees, particularly in the CIB business. The restructuring relating to the ongoing implementation of the RBS Group's strategic programme may cause experienced staff members to leave and prospective staff members not to join the RBS Group.

The lack of continuity of senior management and the loss of important personnel coordinating certain or several aspects of the RBS Group's restructuring could have an adverse impact on its implementation. The failure to attract or retain a sufficient number of appropriately skilled personnel to manage the complex restructuring required to implement the RBS Group's strategy could prevent the RBS Group from successfully implementing its strategy and meeting regulatory commitments. This could have a material adverse effect on the RBS Group's and/or the Group's business, financial condition and results of operations.

In addition, many of the RBS Group's employees in the UK, continental Europe and other jurisdictions in which the RBS Group operates are represented by employee representative bodies, including trade unions. Engagement with its employees and such bodies is important to the RBS Group and a breakdown of these relationships could adversely affect the RBS Group's and/or the Group's business, reputation and results.

HM Treasury (or UKFI on its behalf) may be able to exercise a significant degree of influence over the RBS Group and any further offer or sale of its interests may affect the price of securities issued by the RBS Group.

On 6 August 2015, the UK Government made its first sale of RBSG ordinary shares since its original investment in 2009 and sold approximately 5.4% of its stake in RBSG. Following this initial sale, the UK Government exercised its conversion rights under the B Shares on 14 October 2015 which resulted in HM Treasury holding 72.88% of the ordinary share capital of RBSG. The UK Government, through HM Treasury, currently holds 72.6% of the issued ordinary share capital of RBSG. The UK Government has indicated its intention to continue to sell down its shareholding in the RBS Group over the next five years. Any offers or sale, or expectations relating to the timing thereof, of a substantial number of ordinary shares by HM Treasury, could negatively affect prevailing market prices for the outstanding ordinary shares of RBSG and other securities issued by RBS Group entities and lead to a period of increased price volatility for such securities.

In addition, UKFI manages HM Treasury's shareholder relationship with the RBS Group and, although HM Treasury has indicated that it intends to respect the commercial decisions of the RBS Group and that the RBS Group will continue to have its own independent board of directors and management team determining its own strategy, should HM Treasury's intentions change, its position as a majority shareholder (and UKFI's position as manager of this shareholding) means that HM Treasury or UKFI might be able to exercise a significant degree of influence over, among other things, the election of directors and appointment of senior management, dividend policy, remuneration policy or the conduct of the RBS Group's operations. The manner in which HM Treasury or UKFI exercises HM Treasury's rights as majority shareholder could give rise to conflicts between the interests of HM Treasury and the interests of other shareholders. The Board has a duty to promote the success of the RBS Group for the benefit of its members as a whole.

The RBS Group's earnings and financial condition have been, and its future earnings and financial condition may continue to be, materially affected by depressed asset valuations resulting from poor market conditions.

The RBS Group's businesses are inherently subject to risks in financial markets and in the wider economy, including changes in, and increased volatility of, interest rates, inflation rates, credit spreads, foreign exchange rates and commodity, equity, bond and property prices. In previous years, severe market events resulted in the RBS Group recording large write-downs on its credit market exposures.

Any further deterioration in economic and financial market conditions or weak economic growth could lead to additional impairment charges and write-downs. Moreover, market volatility and illiquidity (and the assumptions, judgements and estimates in relation to such matters that may change over time and may ultimately not turn out to be accurate) make it difficult to value certain of the RBS Group's exposures.

Valuations in future periods reflecting, among other things, the then-prevailing market conditions and changes in the credit ratings of certain of the RBS Group's assets may result in significant changes in the fair values of the RBS Group's exposures, such as credit market exposures, and the value ultimately realised by the RBS Group may be materially different from the current or estimated fair value.

As part of its strategic programme, the RBS Group is executing the run-down or disposal of a number of businesses, assets and portfolios, the most important of which is the divestment of the William & Glyn business which may be carried out as a trade sale or through an IPO. The disposal of Williams & Glyn could lead the RBS Group to recognise further write-downs in the event that the sale proceeds are less than the carrying value of Williams & Glyn in the RBS Group's accounts. In addition, the RBS Group's interest in the remainder of the businesses and portfolios within the exiting business may be difficult to sell due to unfavourable market conditions for such assets or businesses.

Any of these factors could require the RBS Group and/or the Group to recognise further significant write-downs and realise increased impairment charges or goodwill impairments, all of which may have a material adverse effect on their financial condition, results of operations and capital ratios.

The financial performance of the RBS Group has been, and may continue to be, materially affected by customer and counterparty credit quality and deterioration in credit quality could arise due to prevailing economic and market conditions and legal and regulatory developments.

The RBS Group has exposure to many different industries, customers and counterparties, and risks arising from actual or perceived changes in credit quality and the recoverability of monies due from borrowers and other counterparties are inherent in a wide range of the RBS Group's businesses.

In particular, the RBS Group has significant exposure to certain individual customers and other counterparties in weaker business sectors and geographic markets and also has concentrated country exposure in the UK, the US and across the rest of Europe principally Germany, the Netherlands, Ireland and France. At 31 December 2015, credit risk assets in the UK were £311.4 billion, in the US were £24.6 billion and in Western Europe (excluding the UK) were £84.5 billion); and within certain business sectors, namely personal finance, financial institutions, commercial real estate, shipping and the oil and gas sector (at 31 December 2015, personal finance lending amounted to £155.3 billion, lending to financial institutions was £73.1 billion, commercial real estate lending was £27.6 billion, lending to the oil and gas sector was £3.5 billion and shipping was £7.1 billion).

Provisions for default on loans have decreased in recent years in line with the perceived reduction in risks relating to these customers, counterparties or assets classes. If the risk profile of these loans were to increase, including as a result of a degradation of economic or market conditions, this could result in an increase in the cost of risk and the RBS Group and/or the Group may be required to make additional provisions, which in turn would reduce earnings and impact the RBS Group's and/or the Group's profitability.

The RBS Group's lending strategy or processes may also fail to identify or anticipate weaknesses or risks in a particular sector, market or borrower category, which may result in an increase in default rates, which may, in turn, impact the RBS Group's and/or the Group's profitability.

In addition, as the RBS Group implements its new strategy and withdraws from many geographic markets and continues to materially scale down its international activities, the RBS Group's relative exposure to the UK and certain sectors and asset classes in the UK will increase significantly as its business becomes more concentrated in the UK. In particular, in the UK the RBS Group is at risk from volatility in property prices in both the residential and commercial sectors. With UK home loans representing the most significant portion of the RBS Group's total loans and advances to the retail sector, the RBS Group has a large exposure to adverse developments in the UK retail property sector. As a result, a fall in house prices, particularly in London and the South East of the UK, would be likely to lead to higher impairment and negative capital impact as loss given default rate increases. In addition, reduced affordability of residential and commercial property in the UK, for example, as a result of higher interest rates or increased unemployment, could also lead to higher impairment.

The credit quality of the RBS Group's and the Group's borrowers and other counterparties is impacted by prevailing economic and market conditions and by the legal and regulatory landscape in their respective markets. Credit quality has improved in certain of the RBS Group's core markets, in particular the UK and Ireland, as these economies have improved.

However, a further deterioration in economic and market conditions or changes to legal or regulatory landscapes could worsen borrower and counterparty credit quality and also impact the RBS Group's and/or the Group's ability to enforce contractual security rights.

In addition, the RBS Group's and the Group's credit risk is exacerbated when the collateral it holds cannot be realised as a result of market conditions or regulatory intervention or is liquidated at prices not sufficient to recover the full amount of the loan or derivative exposure that is due to them, which is most likely to occur during periods of illiquidity and depressed asset valuations, such as those experienced in recent years. This has particularly been the case with respect to large parts of the RBS Group's commercial real estate portfolio.

Any such deteriorations in the RBS Group's and/or the Group's recoveries on defaulting loans could have an adverse effect on the RBS Group's and/or the Group's results of operations and financial condition.

Concerns about, or a default by, one financial institution could lead to significant liquidity problems and losses or defaults by other financial institutions, as the commercial and financial soundness of many financial institutions may be closely related as a result of credit, trading, clearing and other relationships. Even the perceived lack of creditworthiness of, or questions about, counterparty may lead to market-wide liquidity problems and losses for, or defaults by, the RBS Group. This systemic risk may also adversely affect financial intermediaries, such as clearing agencies, clearing houses, banks, securities firms and exchanges with which the RBS Group interacts on a daily basis. The effectiveness of recent prudential reforms designed to contain systemic risk in the EU and the UK is yet to be tested. Counterparty risk within the financial system or failures of the RBS Group's or the Group's financial counterparties could have a material adverse effect on the RBS Group's or the Group's access to liquidity or could result in losses which could have a material adverse effect on the RBS Group's and/or the Group's financial condition, results of operations and prospects.

The trends and risks affecting borrower and counterparty credit quality have caused, and in the future may cause, the RBS Group and/or the Group to experience further and accelerated impairment charges, increased repurchase demands, higher costs, additional write-downs and losses for the RBS Group and/or the Group and an inability to engage in routine funding transactions.

The RBS Group is committed to executing the run-down and sale of certain businesses, portfolios and assets forming part of the businesses and activities being exited by the RBS Group. Failure by the RBS Group to do so on commercially favourable terms could have a material adverse effect on the RBS Group's operations, operating results, financial position and reputation.

The RBS Group's ability to dispose of the remaining businesses, portfolios and assets forming part of the businesses and activities being exited by the RBS Group and the price achieved for such disposals will be dependent on prevailing economic and market conditions, which remain volatile.

As a result, there is no assurance that the RBS Group will be able to sell, exit or run down these businesses, portfolios or assets either on favourable economic terms to the RBS Group or at all or that it may do so within the intended timetable. Material tax or other contingent liabilities could arise on the disposal or run-down of assets or businesses and there is no assurance that any conditions precedent agreed will be satisfied, or consents and approvals required will be obtained in a timely manner or at all.

The RBS Group may be exposed to deteriorations in the businesses, portfolios or assets being sold between the announcement of the disposal and its completion, which period may span many months.

In addition, the RBS Group may be exposed to certain risks, including risks arising out of ongoing liabilities and obligations, breaches of covenants, representations and warranties, indemnity claims, transitional services arrangements and redundancy or other transaction-related costs, and counterparty risk in respect of buyers of assets being sold.

The occurrence of any of the risks described above could have a material adverse effect on the RBS Group's business, results of operations, financial condition and capital position and consequently may have the potential to impact the competitive position of part or all of the RBS Group's business.

The value or effectiveness of any credit protection that the RBS Group has purchased depends on the value of the underlying assets and the financial condition of the insurers and counterparties.

The RBS Group has some remaining credit exposure arising from over-the-counter derivative contracts, mainly credit default swaps ("CDSs"), and other credit derivatives, each of which are carried at fair value.

The fair value of these CDSs, as well as the RBS Group's or the Group's exposure to the risk of default by the underlying counterparties, depends on the valuation and the perceived credit risk of the instrument against which protection has been bought. Many market counterparties have been adversely affected by their exposure to residential mortgage-linked and corporate credit products, whether synthetic or otherwise, and their actual and perceived creditworthiness may deteriorate rapidly. If the financial condition of these counterparties or their actual or perceived creditworthiness deteriorates, the RBS Group and/or the Group may record further credit valuation adjustments on the credit protection bought from these counterparties under the CDSs.

The RBS Group and the Group also recognise any fluctuations in the fair value of other credit derivatives. Any such adjustments or fair value changes may have a material adverse impact on the RBS Group's and the Group's financial condition and results of operations.

The RBS Group relies on valuation, capital and stress test models to conduct its business, assess its risk exposure and anticipate capital and funding requirements. Failure of these models to provide accurate results or accurately reflect changes in the micro-and macroeconomic environment in which the RBS Group operates could have a material adverse effect on the RBS Group's and/or the Group's business, capital and results.

Given the complexity of the RBS Group's business, strategy and capital requirements, the RBS Group relies on analytical models to manage its business, assess the value of its assets and its risk exposure and anticipate capital and funding requirements, including with stress testing. The RBS Group's valuation, capital and stress test models and the parameters and assumptions on which they are based, need to be constantly updated to ensure their accuracy.

Failure of these models to accurately reflect changes in the environment in which the RBS Group operates, or to be updated in line with the RBS Group's business model or operations, or the failure to properly input any such changes could have an adverse impact on the modelled results or could fail to accurately capture the RBS Group's risk exposure or the risk profile of the RBS Group's financial instruments or result in the RBS Group being required to hold additional capital as a function of the PRA Buffer. In addition, a number of internal models used by the Group are designed, managed and analysed by the RBS Group and may not appropriately capture risks and exposures of the Group. The RBS Group's internal models are subject to periodic review by its regulators and, if found deficient, the RBS Group may be required to make changes to such models or may be precluded from using any such models, which would result in an additional capital requirement that could have a material impact on the RBS Group's capital position. Some of the analytical models used by the RBS Group are predictive in nature. The use of predictive models has inherent risks and may incorrectly forecast future behaviour, leading to flawed decision making and potential losses.

The RBS Group also uses valuation models that rely on market data inputs. If incorrect market data is input into a valuation model, it may result in incorrect valuations or valuations different to those which were predicted and used by the RBS Group in its forecasts or decision making. Internal stress test models may also rely on different, less severe, assumptions or take into account different data points than those defined by the RBS Group's regulators. The RBS Group could face adverse consequences as a result of decisions which may lead to actions by management based on models that are poorly developed, implemented or used, or as a result of the modelled outcome being misunderstood or such information being used for purposes for which it was not designed. Risks arising from the use of models could have a material adverse effect on the RBS Group's and/or the Group's business, financial condition and/or results of operations, minimum capital requirements and reputation.

The reported results of the RBS Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Its results in future periods may be affected by changes to applicable accounting rules and standards.

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses. Due to the inherent uncertainty in making estimates, results reported in future periods may reflect amounts which differ from those estimates. Estimates, judgements and assumptions take into account historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The accounting policies deemed critical to the RBS Group's results and financial position, based upon materiality and significant judgements and estimates, include pensions, goodwill, provisions for liabilities, deferred tax, loan impairment provisions, fair value of financial instruments, which are discussed in detail in "Critical accounting policies and key sources of estimation uncertainty" on page 158. In addition, further development of standards and interpretations under IFRS could also significantly impact the financial results, condition and prospects of the RBS Group and the Group. IFRS and Interpretations that have been issued by the International Accounting Standards Board ("the IASB") but which have not yet been adopted by the Group are discussed in "Accounting developments" on page 160.

In July 2014, the IASB published a new accounting standard for financial instruments (IFRS 9) effective for annual periods beginning on or after 1 January 2018. It introduces a new framework for the recognition and measurement of credit impairment based on expected credit losses, rather than the incurred loss model currently applied under IAS 39. The inclusion of loss allowances with respect to all financial assets will tend to result in an increase in overall impairment balances when compared with the existing basis of measurement under IAS 39.

The valuation of financial instruments, including derivatives, measured at fair value can be subjective, in particular where models are used which include unobservable inputs. Generally, to establish the fair value of these instruments, the Group relies on quoted market prices or, where the market for a financial instrument is not sufficiently active, internal valuation models that utilise observable market data. In certain circumstances, the data for individual financial instruments or classes of financial instruments utilised by such valuation models may not be available or may become unavailable due to prevailing market conditions. In such circumstances, the RBS Group's internal valuation models require the Group to make assumptions, judgements and estimates to establish fair value, which are complex and often relate to matters that are inherently uncertain. Resulting changes in the fair values of the financial instruments has had and could continue to have a material adverse effect on the RBS Group's and/or the Group's earnings, financial condition and capital position.

The RBS Group and its subsidiaries (including the Bank) are subject to a new and evolving framework on recovery and resolution, the impact of which remains uncertain, and which may result in additional compliance challenges and costs.

In the EU, the UK and the US, regulators have implemented or are in the process of implementing recovery and resolution regimes designed to prevent the failure of financial institutions and resolution tools to ensure the timely and orderly resolution of financial institutions. These initiatives are coupled with a broader set of initiatives to improve the resilience of financial institutions and reduce systemic risk, including the UK ring-fencing regime, the introduction of certain requirements and powers under CRD IV, including the rules relating to MDA, and certain of the measures introduced under the BRRD which came into force on 1 January 2015, including the requirements relating to MREL.

The tools and powers introduced under the BBRD include preparatory and preventive measures, early supervisory intervention powers and resolution tools. In addition, banks headquartered in countries which are members of the eurozone are now subject to the European banking union framework.

In November 2014, the ECB assumed direct supervisory responsibility for RBS NV and Ulster Bank Ireland Limited under the Single Supervisory Mechanism ("SSM"). As a result of the above, there remains uncertainty as to how the relevant resolution regimes in force in the UK, the eurozone and other jurisdictions, would interact in the event of a resolution of the RBS Group.

In the UK, the BRRD came into effect in January 2015, subject to certain secondary rules being finalised by the European authorities, and therefore the requirements to which the RBS Group is subject may continue to evolve to ensure compliance with these rules or following the publication of review reports produced by the European Parliament and the Council of the EU relating to certain topics set out by the BRRD. Such further amendments to the BRRD or the implementing rules in the EU may also be necessary to ensure continued consistency with the FSB recommendations on resolution regimes and resolution planning for GSIBs, in particular with respect to TLAC requirements. In addition, the PRA is currently consulting on a new framework requiring financial institutions to ensure the continuity of critical shared services (provided by entities within the RBS Group or external providers) to facilitate recovery action, orderly resolution and post-resolution restructuring, which will apply from 1 January 2019.

The application of such rules to the RBS Group may require the RBS Group to restructure certain of its activities or reorganise the legal structure of its operations, may limit the RBS Group's ability to outsource certain functions and/or may result in increased costs resulting from the requirement to ensure the financial and operational resilience and independent governance of such critical services. Such rules will need to be implemented consistently with the UK ring-fencing regime.

The BRRD requires national resolution funds to raise "ex ante" contributions on banks and investment firms in proportion to their liabilities and risk profiles and allow them to raise additional "ex post" funding contributions in the event the ex ante contributions do not cover the losses, costs or other expenses incurred by use of the resolution fund. Although the UK government indicated that it would consider using receipts from the UK bank levy to meet the ex ante and ex post funding requirements, the RBS Group may be required to make additional contributions in the future. In addition, RBS Group entities in countries subject to the European banking union are required to pay supervisory fees towards the funding of the SSM as well as contributions to the single resolution fund.

The new recovery and resolution regime implementing the BRRD in the UK replaces the previous regime and has imposed and is expected to impose in the near-to medium-term future, additional compliance and reporting obligations on the RBS Group which may result in increased costs, including as a result of the RBS Group's mandatory participation in resolution funds, and heightened compliance risks and the RBS Group may not be in a position to comply with all such requirements within the prescribed deadlines or at all. The implementation of this new regime has required and will continue to require the RBS Group to work with its regulators towards putting in place adequate resolution plans, the outcome of which may impact the RBS Group's operations or structure.

The RBS Group may become subject to the application of stabilisation or resolution powers in certain significant stress situations, which may result in various actions being taken in relation to the RBS Group and any securities of the RBS Group, including the write-off, write-down or conversion of the RBS Group's securities.

In the context of the recovery and resolution framework set out above, as the parent company of a UK bank, RBSG is subject to the "Special Resolution Regime" under the Banking Act 2009, that gives wide powers to HM Treasury, the Bank of England, the PRA and the FCA in circumstances where a UK bank has encountered or is likely to encounter financial difficulties, such that it is assessed as failing or likely to fail.

The Special Resolution Regime under the Banking Act 2009, as amended to implement the relevant provisions of the BRRD in the UK from 1 January 2015, includes powers to (a) transfer all or some of the securities issued by a UK bank or its parent, or all or some of the property, rights and liabilities of a UK bank or its parent, to a commercial purchaser or, transfer of the bank into temporary public ownership, or, in the case of property, rights or liabilities, to a bridge bank (an entity owned by the Bank of England); (b) together with another resolution tool only, transfer impaired or problem assets to one or more publicly owned asset management vehicles; (c) override any default provisions, contracts or other agreements, including provisions that would otherwise allow a party to terminate a contract or accelerate the payment of an obligation; (d) commence certain insolvency procedures in relation to a UK bank; and (e) override, vary or impose contractual obligations, for reasonable consideration, between a UK bank or its parent and its group undertakings (including undertakings which have ceased to be members of the group), in order to enable any transferee or successor bank of the UK bank to operate effectively. Where stabilisation options are used under (a) or (b) above which rely on the use of public funds, the option can only be used once there has been a contribution to loss absorption and recapitalisation of at least 8% of the total liabilities of the institution under resolution.

In addition, among the changes introduced by the Banking Reform Act 2013 and amendments made subsequently to implement the relevant provisions of the BRRD, the Banking Act 2009 was amended to insert a bail-in power as part of the powers available to the UK resolution authority.

The bail-in power includes both a capital instruments write-down and conversion power applicable to Tier 1 and Tier 2 instruments and triggered at the point of non-viability of a financial institution and a bail-in tool applicable to eligible liabilities (including the senior unsecured debt securities issued by the RBS Group) and available in resolution.

The capital instruments write-down and conversion power may be exercised independently of, or in combination with, the exercise of a resolution tool (other than the bail-in tool, which would be used instead of the capital instruments write-down and conversion power), and it allows resolution authorities to cancel all or a portion of the principal amount of capital instruments and/or convert such capital instruments into common equity Tier 1 instruments when an institution is no longer viable. The point of non-viability for such purposes is the point at which the Bank of England or the PRA determines that the institution meets the conditions for entry into the Special Resolution Regime as defined under the Banking Act 2009 or will no longer be viable unless the relevant capital instruments are written down or extraordinary public support is provided, and without such support the appropriate authority determines that the institution would no longer be viable.

Where the conditions for resolution exist and it is determined that a stabilisation power may be exercised, the Bank of England may use the bail-in tool (in combination with other resolution tools under the Banking Act 2009) to, among other things, cancel or reduce all or a portion of the principal amount of, or interest on, certain unsecured liabilities of a failing financial institution and/or convert certain debt claims into another security, including ordinary shares of the surviving entity. In addition, the Bank of England may use the bail-in tool to, among other things, replace or substitute the issuer as obligor in respect of debt instruments, modify the terms of debt instruments (including altering the maturity (if any) and/or the amount of interest payable and/or imposing a temporary suspension on payments) and discontinue the listing and admission to trading of financial instruments.

The exercise of the bail-in tool will be determined by the Bank of England which will have discretion to determine whether the institution has reached a point of non-viability or whether the conditions for resolution are met, by application of the relevant provisions of the Banking Act 2009, and involves decisions being taken by the PRA and the Bank of England, in consultation with the FCA and HM Treasury. As a result, it will be difficult to predict when, if at all, the exercise of the bail-in power may occur.

The potential impact of these powers and their prospective use may include increased volatility in the market price of shares and other securities issued by the RBS Group, as well as increased difficulties in issuing securities in the capital markets and increased costs of raising such funds. If these powers were to be exercised (or there is an increased risk of exercise) in respect of the RBS Group or any entity within the RBS Group (including the Bank) such exercise could result in a material adverse effect on the rights or interests of shareholders which would likely be extinguished or very heavily diluted.

Holders of debt securities (which may include holders of senior unsecured debt), would see the conversion of part (or all) of their claims into equity or written down in part or written off entirely. In accordance with the rules of the Special Resolution Regime, the losses imposed on holders of equity and debt instruments through the exercise of bail-in powers would be subject to the "no creditor worse off" safeguard, which requires losses not to exceed those which would be realised in insolvency.

In the UK and in other jurisdictions, the RBS Group is responsible for contributing to compensation schemes in respect of banks and other authorised financial services firms that are unable to meet their obligations to customers.

In the UK, the Financial Services Compensation Scheme (FSCS) was established under the FSMA and is the UK's statutory fund of last resort for customers of authorised financial services firms.

The FSCS can pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it and may be required to make payments either in connection with the exercise of a stabilisation power or in exercise of the bank insolvency procedures under the Banking Act 2009. The FSCS is funded by levies on firms authorised by the FCA, including the RBS Group. In the event that the FSCS raises funds from the authorised firms, raises those funds more frequently or significantly increases the levies to be paid by such firms, the associated costs to the RBS Group may have an adverse impact on its and/or the Group's results of operations and financial condition. To the extent that other jurisdictions where the RBS Group operates have introduced or plan to introduce similar compensation, contributory or reimbursement schemes, the RBS Group may make further provisions and may incur additional costs and liabilities, which may have an adverse impact on its financial condition and results of operations.

The RBS Group's results could be adversely affected in the event of goodwill impairment.

The RBS Group capitalises goodwill, which is calculated as the excess of the cost of an acquisition over the net fair value of the identifiable assets, liabilities and contingent liabilities acquired. Acquired goodwill is recognised initially at cost and subsequently at cost less any accumulated impairment losses. As required by IFRS, the RBS Group tests goodwill for impairment annually, or more frequently when events or circumstances indicate that it might be impaired.

An impairment test involves comparing the recoverable amount (the higher of the value in use and fair value less cost to sell) of an individual cash generating unit with its carrying value.

At 31 December 2015, the RBS Group carried goodwill of £5.6 billion on its balance sheet, taking into account an impairment charge of £498 million in respect of Private Banking in Q4 2015 which was made in light of a number of factors, including a reduction in anticipated future profitability due to the continuing low interest rate environment, a higher tax rate, margin pressure and higher capital allocations. The value in use and fair value of the RBS Group's cash-generating units are affected by market conditions and the performance of the economies in which the RBS Group operates.

Where the RBS Group is required to recognise a goodwill impairment, it is recorded in the RBS Group's income statement, but it has no effect on the RBS Group's regulatory capital position. Further impairments of the RBS Group's goodwill could have an adverse effect on the RBS Group's results and financial condition.

Recent changes in the tax legislation in the UK are likely to result in increased tax payments by the RBS Group and may impact the recoverability of certain deferred tax assets recognised by the RBS Group.

In accordance with IFRS, the RBS Group has recognised deferred tax assets on losses available to relieve future profits from tax only to the extent it is probable that they will be recovered. The deferred tax assets are quantified on the basis of current tax legislation and accounting standards and are subject to change in respect of the future rates of tax or the rules for computing taxable profits and offsetting allowable losses.

The Finance Act 2015 included new restrictions on the use of certain brought forward tax losses of banking companies to 50% of relevant profits from 1 April 2015, which has impacted the extent to which the RBS Group is able to recognise deferred tax assets and has been reflected in its year-end accounts. At 31 December 2015, the RBS Group recognised a net deferred tax asset (taking account of the Finance Act 2015 changes) of £2.6 billion. On 16 March 2016, the UK Government announced their intention to further restrict the use of tax losses carried forward by UK banks. If these measures are enacted by the UK Parliament during the course of 2016, a longer recovery period of the deferred tax assets associated with UK tax losses will therefore arise. Failure to generate sufficient future taxable profits or further changes in tax legislation (including rates of tax) or accounting standards may reduce the recoverable amount of the recognised deferred tax assets. Further changes to the treatment of deferred tax assets may impact the RBS Group's capital, for example by reducing further the RBS Group's ability to recognise deferred tax assets. Further, the new 8% tax surcharge which applies to banking companies from 1 January 2016 cannot be offset by brought forward tax losses arising before this time, or by any tax losses arising in non-banking companies within the RBS Group. In addition, the implementation of the rules relating to the UK ring- fencing regime and the resulting restructuring of the RBS Group may further restrict the RBS Group's ability to recognise tax deferred tax assets in respect of brought forward losses.

Abbreviations and acronyms

ABS	Asset-backed securities
AFS	Available-for-sale
AQ	Asset quality
AT1	Additional Tier 1
BCBS	Basel Committee on Banking Supervision
C&RA	Conduct & Regulatory Affairs
CDO	Collateralised debt obligation
CDS	Credit default swap
CET1	Common equity tier 1
CFG	Citizens Financial Group Inc.
CIB	Corporate & Institutional Banking
CLO	Collateralised loan obligation
CMBS	Commercial mortgage-backed securities
CPB	Commercial & Private Banking
CRD	Capital Requirements Directive
CRE	Commercial real estate
CVA	Credit valuation adjustment
DFV	Designated as at fair value through profit or loss
EAD	Exposure at default
EBA	European Banking Authority
EC	European Commission
EMEA	Europe, the Middle East and Africa
ERF	Executive Risk Forum
EU	European Union
FCA	Financial Conduct Authority
FI	Financial institution
FSA	Financial Services Authority
FSB	Financial Stability Board
FSCS	Financial Services Compensation Scheme
FVTPL	Fair value through profit or loss
GDP	Gross domestic product
GSIB	Global systemically important bank
HFT	Held-for-trading
HMT	HM Treasury
HTM	Held-to-maturity
IAS	International Accounting Standards
IASB	International Accounting Standards Board
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
IPV	Independent price verification
IRC	Incremental risk charge
LAR	Loans and receivables
LCR	Liquidity coverage ratio
LIBOR	London Interbank Offered Rate
LGD	Loss given default
LTI	Long term incentive awards
LTV	Loan-to-value
MDA	Maximum distributable amount
NI	Northern Ireland
NSFR	Net stable funding ratio
PBB	Personal & Business Banking
PD	Probability of default
PPI	Payment Protection Insurance
PRA	Prudential Regulation Authority
RBSG	The Royal Bank of Scotland Group plc
RCR	RBS Capital Resolution
REIL	Risk elements in lending
RFS	RFS Holdings B.V.
RMBS	Residential mortgage-backed securities
RNIV	Risks not In VaR
ROI	Republic of Ireland
RoW	Rest of the World
RWA	Risk-weighted asset
SE	Structured entity
SEC	US Securities and Exchange Commission
SME	Small and medium-sized enterprise
SVaR	Stressed value-at-risk
TLAC	Total loss absorbing capacity
TSR	Total Shareholder Return
UK	United Kingdom
UKFI	UK Financial Investments Limited
US/USA	United States of America
VaR	Value-at-risk

In the Report and Accounts, and unless specified otherwise, the terms 'the Royal Bank', 'RBS plc' or 'the Bank' mean The Royal Bank of Scotland plc, the 'Group' means the Bank and its subsidiaries, 'RBSG' or the 'holding company' mean The Royal Bank of Scotland Group plc' and 'RBS Group' means the holding company and its subsidiaries, and 'NatWest' means National Westminster Bank Plc.

The bank publishes its financial statements in pounds sterling ('£' or 'sterling'). The abbreviations '£m' and '£bn' represent millions and thousands of millions of pounds sterling, respectively, and references to 'pence' represent pence in the United Kingdom ('UK'). Reference to 'dollars' or '$' are to United States of America ('US') dollars. The abbreviations '$m' and '$bn' represent millions and thousands of millions of dollars, respectively, and references to 'cents' represent cents in the US. The abbreviation '€' represents the 'euro', and the abbreviations '€m' and '€bn' represent millions and thousands of millions of euros, respectively

Glossary of terms

Arrears - the aggregate of contractual payments due on a debt that have not been met by the borrower. A loan or other financial asset is said to be 'in arrears' when payments have not been made.

Asset-backed commercial paper (ABCP) - a form of asset-backed security generally issued by a commercial paper conduit.

Asset-backed securities (ABS) - securities that represent interests in specific portfolios of assets. They are issued by a structured entity following a securitisation. The underlying portfolios commonly comprise residential or commercial mortgages but can include any class of asset that yields predictable cash flows. Payments on the securities depend primarily on the cash flows generated by the assets in the underlying pool and other rights designed to assure timely payment, such as guarantees or other credit enhancements. Collateralised debt obligations, collateralised loan obligations, commercial mortgage backed securities and residential mortgage backed securities are all types of ABS.

Asset quality (AQ) band - probability of default banding for all counterparties on a scale of 1 to 10.

Assets under management - assets managed by the Group on behalf of clients.

Back-testing - statistical techniques that assess the performance of a model, and how that model would have performed had it been applied in the past.

Basel II - the capital adequacy framework issued by the Basel Committee on Banking Supervision in June 2006 in the form of the 'International Convergence of Capital Measurement and Capital Standards'.

Basel III - in December 2010, the Basel Committee on Banking Supervision issued final rules: 'Basel III: A global regulatory framework for more resilient banks and banking systems' and 'Basel III: International framework for liquidity risk measurement, standards and monitoring'.

Basis point - one hundredth of a per cent i.e. 0.01 per cent. 100 basis points is 1 per cent. Used when quoting movements in interest rates or yields on securities.

Buy-to-let mortgages - mortgages to customers for the purchase of residential property as a rental investment.

Capital requirements regulation (CRR) - refer to CRD IV.

Central counterparty (CCP) - an intermediary between a buyer and a seller (generally a clearing house).

Certificates of deposit (CDs) - bearer negotiable instruments acknowledging the receipt of a fixed term deposit at a specified interest rate.

Collateralised debt obligations (CDOs) - asset-backed securities for which the underlying asset portfolios are debt obligations: either bonds (collateralised bond obligations) or loans (collateralised loan obligations) or both. The credit exposure underlying synthetic CDOs derives from credit default swaps. The CDOs issued by an individual vehicle are usually divided in different tranches: senior tranches (rated AAA), mezzanine tranches (AA to BB), and equity tranches (unrated). Losses are borne first by the equity securities, next by the junior securities, and finally by the senior securities; junior tranches offer higher coupons (interest payments) to compensate for their increased risk.

Collateralised loan obligations (CLOs) - asset-backed securities for which the underlying asset portfolios are loans, often leveraged loans.

Collectively assessed loan impairment provisions - impairment loss provisions in respect of impaired loans, such as credit cards or personal loans, that are below individual assessment thresholds. Such provisions are established on a portfolio basis, taking account of the level of arrears, security, past loss experience, credit scores and defaults based on portfolio trends.

Commercial mortgage backed securities (CMBS) - asset-backed securities for which the underlying asset portfolios are loans secured on commercial real estate.

Commercial paper (CP) - unsecured obligations issued by a corporate or a bank directly or secured obligations (asset-backed CP), often issued through a commercial paper conduit, to fund working capital. Maturities typically range from two to 270 days. However, the depth and reliability of some CP markets means that issuers can repeatedly roll over CP issuance and effectively achieve longer term funding. CP is issued in a wide range of denominations and can be either discounted or interest-bearing.

Commercial paper conduit - a structured entity that issues commercial paper and uses the proceeds to purchase or fund a pool of assets. The commercial paper is secured on the assets and is redeemed either by further commercial paper issuance, repayment of assets or liquidity drawings.

Commercial real estate - freehold and leasehold properties used for business activities. Commercial real estate includes office buildings, industrial property, medical centres, hotels, retail stores, shopping centres, agricultural land and buildings, warehouses, garages etc.

Common Equity Tier 1 capital - the highest quality form of regulatory capital under Basel III comprising common shares issued and related share premium, retained earnings and other reserves excluding reserves which are restricted or not immediately available, less specified regulatory adjustments.

Contractual maturity - the date in the terms of a financial instrument on which the last payment or receipt under the contract is due for settlement.

Glossary of terms

Cost:income ratio - operating expenses as a percentage of total income.

Counterparty credit risk - the risk that a counterparty defaults before the maturity of a derivative or sale and repurchase contract. In contrast to non-counterparty credit risk, the exposure to counterparty credit risk varies by reference to a market factor (e.g. interest rate, exchange rate, asset price).

Coverage ratio - impairment provisions as a percentage of impaired loans.

Covered bonds - debt securities backed by a portfolio of mortgages that are segregated from the issuer's other assets solely for the benefit of the holders of the covered bonds.

CRD IV - the European Union has implemented the Basel III capital proposals through the CRR and the CRD, collectively known as CRD IV. CRD IV was implemented on 1 January 2014. The EBA's technical standards are still to be finalised through adoption by the European Commission and implemented within the UK.

Credit default swap (CDS) - a contract where the protection seller receives premium or interest-related payments in return for contracting to make payments to the protection buyer upon a defined credit event in relation to a reference financial asset or portfolio of financial assets. Credit events usually include bankruptcy, payment default and rating downgrades.

Credit derivative product company (CDPC) - a structured entity that sells credit protection under credit default swaps or certain approved forms of insurance policies. CDPCs are similar to monoline insurers. However, unlike monoline insurers, they are not regulated as insurers.

Credit derivatives - contractual agreements that provide protection against a credit event on one or more reference entities or financial assets. The nature of a credit event is established by the protection buyer and protection seller at the inception of a transaction, and such events include bankruptcy, insolvency or failure to meet payment obligations when due. The buyer of the credit derivative pays a periodic fee in return for a payment by the protection seller upon the occurrence of a credit event. Credit derivatives include credit default swaps, total return swaps and credit swap options.

Credit enhancements - techniques that improve the credit standing of financial obligations; generally those issued by a structured entity in a securitisation. External credit enhancements include financial guarantees and letters of credit from third party providers. Internal enhancements include excess spread - the difference between the interest rate received on the underlying portfolio and the coupon on the issued securities; and over-collateralisation – at inception, the value of the underlying portfolio is greater than the securities issued.

Credit grade - a rating that represents an assessment of the creditworthiness of a customer. It is a point on a scale representing the probability of default of a customer.

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

Credit risk mitigation - reducing the credit risk of an exposure by application of techniques such as netting, collateral, guarantees and credit derivatives.

Credit valuation adjustment (CVA) - the CVA is the difference between the risk-free value of a portfolio of trades and its market value, taking into account the counterparty's risk of default. It represents the market value of counterparty credit risk, or an estimate of the adjustment to fair value that a market participant would make to reflect the creditworthiness of its counterparty.

Currency swap - an arrangement in which two parties exchange specific principal amounts of different currencies at inception and subsequently interest payments on the principal amounts. Often, one party will pay a fixed rate of interest, while the other will pay a floating rate (though there are also fixed-fixed and floating-floating currency swaps). At the maturity of the swap, the principal amounts are usually re-exchanged.

Customer accounts - money deposited with the Group by counterparties other than banks and classified as liabilities. They include demand, savings and time deposits; securities sold under repurchase agreements; and other short term deposits. Deposits received from banks are classified as deposits by banks.

Debit valuation adjustment (DVA) - an adjustment made in valuing OTC derivative liabilities to reflect the entity's own credit risk.

Debt securities - transferable instruments creating or acknowledging indebtedness. They include debentures, bonds, certificates of deposit, notes and commercial paper. The holder of a debt security is typically entitled to the payment of principal and interest, together with other contractual rights under the terms of the issue, such as the right to receive certain information. Debt securities are generally issued for a fixed term and redeemable by the issuer at the end of that term. Debt securities can be secured or unsecured.

Debt securities in issue - unsubordinated debt securities issued by the Group. They include commercial paper, certificates of deposit, bonds and medium-term notes.

Deferred tax asset - income taxes recoverable in future periods as a result of deductible temporary differences (temporary differences between the accounting and tax base of an asset or liability that will result in tax deductible amounts in future periods) and the carry-forward of tax losses and unused tax credits.

Glossary of terms

Deferred tax liability - income taxes payable in future periods as a result of taxable temporary differences (temporary differences between the accounting and tax base of an asset or liability that will result in taxable amounts in future periods).

Defined benefit obligation - the present value of expected future payments required to settle the obligations of a defined benefit plan resulting from employee service.

Defined benefit plan/scheme - pension or other post-retirement benefit plan other than a defined contribution plan.

Defined contribution plan/scheme - pension or other post-retirement benefit plan where the employer's obligation is limited to its contributions to the fund.

Deposits by banks - money deposited with the Group by banks and recorded as liabilities. They include money-market deposits, securities sold under repurchase agreements, federal funds purchased and other short term deposits. Deposits received from customers are recorded as customer accounts.

Derivative - a contract or agreement whose value changes with changes in an underlying variable such as interest rates, foreign exchange rates, share prices or indices and which requires no initial investment or an initial investment that is smaller than would be required for other types of contracts with a similar response to market factors. The principal types of derivatives are: swaps, forwards, futures and options.

Discontinued operation - a component of the Group that either has been disposed of or is classified as held for sale. A discontinued operation is either: a separate major line of business or geographical area of operations or part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or a subsidiary acquired exclusively with a view to resale.

Economic capital - an internal measure of the capital required by the Group to support the risks to which it is exposed.

Economic profit - the difference between the return on shareholders funds and the cost of that capital. Economic profit is usually expressed as a percentage.

Effective interest rate method - the effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or liabilities) and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. Calculation of the effective interest rate takes into account fees payable or receivable that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual terms of a financial instrument are considered when estimating future cash flows.

Encumbrance - an interest in an asset held by another party. Encumbrance usually restricts the asset's transferability until the encumbrance is removed.

Equity risk - the risk of changes in the market price of the equities or equity instruments arising from positions, either long or short, in equities or equity-based financial instruments.

Eurozone - the 19 European Union countries that have adopted the euro: Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain.

Expected loss (EL) - expected loss represents the anticipated loss on an exposure over one year. It is determined by multiplying probability of default, loss given default and exposure at default and can be calculated at individual, credit facility, customer or portfolio level.

Exposure - a claim, contingent claim or position which carries a risk of financial loss.

Exposure at default (EAD) - an estimate of the extent to which the bank will be exposed under a specific facility, in the event of the default of a counterparty.

FICO score - a credit score calculated using proprietary software developed by the Fair Isaac Corporation in the US from a consumer's credit profile. The scores range between 300 and 850 and are used in credit decisions made by banks and other providers of credit.

Financial Conduct Authority (FCA) - the statutory body responsible for conduct of business regulation and supervision of UK authorised firms from 1 April 2013. The FCA also has responsibility for the prudential regulation of firms that do not fall within the PRA's scope.

Financial Services Compensation Scheme (FSCS) - the UK's statutory fund of last resort for customers of authorised financial services firms. It pays compensation if a firm is unable to meet its obligations. The FSCS funds compensation for customers by raising management expenses levies and compensation levies on the financial services industry.

First/second lien - a lien is a charge such as a mortgage held by one party, over property owned by a second party, as security for payment of some debt, obligation, or duty owed by that second party. The holder of a first lien takes precedence over all other encumbrances on that property i.e. second and subsequent liens.

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

Forward contract - a contract to buy (or sell) a specified amount of a physical or financial commodity, at an agreed price, at an agreed future date.

Glossary of terms

Futures contract - a contract which provides for the future delivery (or acceptance of delivery) of some type of financial instrument or commodity under terms established at the outset. Futures differ from forward contracts in that they are standardised and traded on recognised exchanges and rarely result in actual delivery; most contracts are closed out prior to maturity by acquisition of an offsetting position.

G10 - the Group of Ten comprises the eleven industrial countries (Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, Switzerland, the United Kingdom and the United States) that have agreed to participate in the International Monetary Fund's (IMF's) General Arrangements to Borrow.

Government Sponsored Enterprises (GSEs) - a group of financial services corporations created by the US Congress. Their function is to improve the efficiency of capital markets and to overcome statutory and other market imperfections which otherwise prevent funds from moving easily from suppliers of funds to areas of high loan demand. They include the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association.

Gross yield - the interest rate earned on average interest-earning assets i.e. interest income divided by average interest-earning assets.

Haircut - a downward adjustment to collateral value to reflect its nature and any currency or maturity mismatches between the collateral and the exposure it secures.

Hedge funds - pooled investment vehicles that are not widely available to the public; their assets are managed by professional asset managers who participate in the performance of the fund.

Impaired loans - all loans for which an impairment provision has been established; for collectively assessed loans, impairment loss provisions are not allocated to individual loans and the entire portfolio is included in impaired loans.

Impairment allowance - refer to Loan impairment provisions.

Impairment losses - (a) for impaired financial assets measured at amortised cost, impairment losses - the difference between carrying value and the present value of estimated future cash flows discounted at the asset's original effective interest rate - are recognised in profit or loss and the carrying amount of the financial asset reduced by establishing a provision (allowance) (b) for impaired available-for-sale financial assets, the cumulative loss that had been recognised directly in equity is removed from equity and recognised in profit or loss as an impairment loss.

Individual liquidity guidance (ILG) - guidance from the PRA on a firm's required quantity of liquidity resources and funding profile.

Individually assessed loan impairment provisions - impairment loss provisions for individually significant impaired loans assessed on a case-by-case basis, taking into account the financial condition of the counterparty and any guarantor and the realisable value of any collateral held.

Interest rate swap - a contract under which two counterparties agree to exchange periodic interest payments on a predetermined monetary principal, the notional amount.

Interest spread - the difference between the gross yield and the interest rate paid on average interest-bearing liabilities.

Internal Capital Adequacy Assessment Process (ICAAP) - the Group's own assessment, as part of Basel III requirements, of its risks, how it intends to mitigate those risks and how much current and future capital is necessary having considered other mitigating factors.

Internal funding of trading business - the internal funding of the trading book comprises net banking book financial liabilities that fund financial assets in the Group's trading portfolios. Interest payable on these financial liabilities is charged to the trading book.

International Accounting Standards Board (IASB) - the independent standard-setting body of the IFRS Foundation. Its members are responsible for the development and publication of International Financial Reporting Standards (IFRSs) and for approving Interpretations of IFRS as developed by the IFRS Interpretations Committee.

International Swaps and Derivatives Association (ISDA) master agreement - a standardised contract developed by ISDA for bilateral derivatives transactions. The contract grants legal rights of set-off for derivative transactions with the same counterparty.

Investment grade - generally represents a risk profile similar to a rating of BBB-/Baa3 or better, as defined by independent rating agencies.

Key management - members of the RBS Group Executive Committee.

Latent loss provisions - loan impairment provisions held against impairments in the performing loan portfolio that have been incurred as a result of events occurring before the balance sheet date but which have not been identified at the balance sheet date.

Level 1 - level 1 fair value measurements are derived from quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date.

Level 2 - level 2 fair value measurements use inputs, other than quoted prices included within level 1, that are observable for the asset or liability, either directly or indirectly.

Level 3 - level 3 fair value measurements use one or more unobservable inputs for the asset or liability.

Leverage ratio - a measure prescribed under Basel III. It is the ratio of Tier 1 capital to total exposures. Total exposures include on-balance sheet items, off-balance sheet items and derivatives, and generally follow the accounting measure of exposure.

Liquidity and funding risk - the risk that the Group is unable to meet its financial liabilities when they fall due.

Glossary of terms

Liquidity coverage ratio (LCR) - the ratio of the stock of high quality liquid assets to expected net cash outflows over the following 30 days. High quality liquid assets should be unencumbered, liquid in markets during a time of stress and, ideally, central bank eligible.

Loan:deposit ratio - the ratio of loans and advances to customers net of provision for impairment losses and excluding reverse repurchase agreements to customer deposits excluding repurchase agreements.

Loan impairment provisions - loan impairment provisions are established to recognise incurred impairment losses on a portfolio of loans classified as loans and receivables and carried at amortised cost. It has three components: individually assessed loan impairment provisions, collectively assessed loan impairment provisions and latent loss provisions.

Loan-to-value ratio - the amount of a secured loan as a percentage of the appraised value of the security e.g. the outstanding amount of a mortgage loan as a percentage of the property's value.

London Interbank Offered Rate (LIBOR) - the benchmark interest rate at which banks can borrow funds from other banks in the London interbank market.

Loss given default (LGD) - an estimate of the amount that will not be recovered by the Group in the event of default, plus the cost of debt collection activities and the delay in cash recovery.

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

Master netting agreement - an agreement between two counterparties that have multiple derivative contracts with each other that provides for the net settlement of all contracts through a single payment, in a single currency, in the event of default on, or termination of, any one contract.

Maximum distributable amount (MDA) - a restriction on distributions which may be made by a bank which does not meet the combined buffer requirements as set out in the PRA Supervisory Statement SS6/14 'Implementing CRD IV: capital buffers'.

Medium term notes (MTNs) - debt securities usually with a maturity of five to ten years, but the term may be less than one year or as long as 50 years. They can be issued on a fixed or floating coupon basis or with an exotic coupon; with a fixed maturity date (non-callable) or with embedded call or put options or early repayment triggers. MTNs are generally issued as senior unsecured debt.

Monoline insurers (monolines) - entities that specialise in providing credit protection against the notional and interest cash flows due to the holders of debt instruments in the event of default. This protection is typically in the form of derivatives such as credit default swaps.

Mortgage-backed securities - asset-backed securities for which the underlying asset portfolios are loans secured on property. See Residential mortgage backed securities and Commercial mortgage backed securities.

Mortgage servicing rights - the rights of a mortgage servicer to collect mortgage payments and forward them, after deducting a fee, to the mortgage lender.

Negative equity mortgages - mortgages where the value of the property mortgaged is less than the outstanding balance on the loan.

Net interest income - the difference between interest receivable on financial assets classified as loans and receivables or available-for-sale and interest payable on financial liabilities carried at amortised cost.

Net interest margin - net interest income as a percentage of average interest-earning assets.

Net stable funding ratio (NSFR) - the ratio of available stable funding to required stable funding over a one year time horizon, assuming a stressed scenario. Available stable funding includes items such as equity capital, preferred stock with a maturity of over one year and liabilities with an assessed maturity of over one year.

Non-performing loans - loans classified as Risk elements in lending and potential problem loans. They have a 100% probability of default and have been assigned an AQ10 internal credit grade.

Operational risk - the risk of loss resulting from inadequate or failed processes, people, systems or from external events.

Option - an option is a contract that gives the holder the right but not the obligation to buy (or sell) a specified amount of an underlying physical or financial commodity, at a specific price, at an agreed date or over an agreed period. Options can be exchange-traded or traded over-the-counter.

Over-the-counter (OTC) derivatives - derivatives with tailored terms and conditions negotiated bilaterally, in contrast to exchange traded derivatives that have standardised terms and conditions.

Own credit adjustment (OCA) - the effect of the Group's own credit standing on the fair value of financial liabilities.

Past due - a financial asset such as a loan is past due when the counterparty has failed to make a payment when contractually due.

Glossary of terms

Pillar 1 - the part of CRD IV that sets out the process by which regulatory capital requirements should be calculated for credit, market and operational risk.

Pillar 2 - Pillar 2 is intended to ensure that firms have adequate capital to support all the relevant risks in their business and is divided into capital held against risks not captured or not fully captured by the Pillar 1 regulations (Pillar 2A) and risks to which a firm may become exposed over a forward-looking planning horizon (Pillar 2B). Capital held under Pillar 2A, in addition to the Pillar 1 requirements, is the minimum level of regulatory capital a bank should maintain at all times to cover adequately the risks to which it is or might be exposed, and to comply with the overall financial adequacy rules. Pillar 2B is a capital buffer which helps to ensure that a bank can continue to meet minimum requirements during a stressed period, and is determined by the PRA evaluating the risks to which the firm may become exposed (e.g. due to changes to the economic environment) during the supervisory review and evaluation process. All firms will be subject to a PRA buffer assessment and the PRA will set a PRA buffer only if it judges that the CRD IV buffers are inadequate for a particular firm given its vulnerability in a stress scenario, or where the PRA has identified risk management and governance failings, which the CRD IV buffers are not intended to address.

Pillar 3 - the part of CRD IV that sets out the information banks must disclose about their risks, the amount of capital required to absorb them, and their approach to risk management. The aim is to strengthen market discipline.

Position risk requirement - a capital requirement applied to a position treated under the Market Risk Rules as part of the calculation of the market risk capital requirement.

Potential future exposure - is a measure of counterparty risk/credit risk. It is calculated by evaluating existing trades done against the possible market prices in future during the lifetime of the transactions.

Potential problem loans (PPL) - loans for which an impairment event has taken place but no impairment loss is expected. This category is used for advances which are not past due 90 days or revolving credit facilities where identification as 90 days overdue is not feasible.

PRA Rule Book - contains provisions made by the PRA that apply to PRA authorised firms. Within 'Banking and Investment Rules', the Capital Requirements firms' section applies to the Group.

Private equity - equity investments in operating companies not quoted on a public exchange. Capital for private equity investment is raised from retail or institutional investors and used to fund investment strategies such as leveraged buyouts, venture capital, growth capital, distressed investments and mezzanine capital.

Probability of default (PD) - the likelihood that a customer will fail to make full and timely repayment of credit obligations over a one year time horizon.

Prudential Regulation Authority (PRA) - the statutory body responsible for the prudential supervision of banks, building societies, insurers and a small number of significant investment firms in the UK. The PRA is a subsidiary of the Bank of England.

Regular way purchase or sale - a purchase or sale of a financial asset under a contract whose terms require delivery of the asset within the time frame established generally by regulation or convention in the marketplace concerned.

Regulatory capital - the amount of capital that the Group holds, determined in accordance with rules established by the PRA for the consolidated Group and by local regulators for individual Group companies.

Repurchase agreement (Repo) - refer to Sale and repurchase agreements.

Residential mortgage - a loan to purchase a residential property where the property forms collateral for the loan. The borrower gives the lender a lien against the property and the lender can foreclose on the property if the borrower does not repay the loan per the agreed terms. Also known as a home loan.

Residential mortgage backed securities (RMBS) - asset-backed securities for which the underlying asset portfolios are residential mortgages. RBS Group RMBS classifications, including prime, non-conforming and sub-prime, reflect the characteristics of the underlying mortgage portfolios. RMBS are classified as prime RMBS where the loans have low default risk and are made to borrowers with good credit records and reliable payment histories and there is full documentation. Non-conforming RMBS include US Alt-A RMBS, together with RMBS in jurisdictions other than the US where the underlying mortgages are not classified as either prime or sub-prime. Classification of RMBS as subprime or Alt-A is based on Fair Isaac Corporation scores (FICO), level of documentation and loan-to-value ratios of the underlying mortgage loans. US RMBS are classified as sub-prime if the mortgage portfolio comprises loans with FICO scores between 500 and 650 with full or limited documentation. Mortgages in Alt-A RMBS portfolios have FICO scores of 640 to 720, limited documentation and an original LTV of 70% to 100%. In other jurisdictions, RMBS are classified as sub-prime if the mortgage portfolio comprises loans with one or more high risk characteristics such as: unreliable or poor payment histories; high loan-to-value ratios; high debt-to-income ratio; the loan is not secured on the borrower's primary residence; or a history of delinquencies or late payments on the loan.

Retail loans - loans made to individuals rather than institutions. The loans may be for car purchases, home purchases, medical care, home repair, holidays and other consumer uses.

Return on equity - profit attributable to ordinary shareholders divided by average shareholders' equity as a percentage.

Reverse repurchase agreement (Reverse repo) - refer to Sale and repurchase agreements.

Risk appetite - an expression of the maximum level of risk that the Group is prepared to accept to deliver its business objectives.

Glossary of terms

Risk asset ratio (RAR) - total regulatory capital as a percentage of risk-weighted assets.

Risk elements in lending (REIL) - impaired loans and accruing loans which are contractually overdue 90 days or more as to principal or interest.

Risk-weighted assets (RWAs) - assets adjusted for their associated risks using weightings established in accordance with the CRD IV as implemented by the PRA. Certain assets are not weighted but deducted from capital.

Sale and repurchase agreements - in a sale and repurchase agreement one party, the seller, sells a financial asset to another party, the buyer, at the same time the seller agrees to reacquire and the buyer to resell the asset at a later date. From the seller's perspective such agreements are repurchase agreements (repos) and from the buyer's reverse repurchase agreements (reverse repos).

Securitisation - a process by which assets or cash flows are transformed into transferable securities. The underlying assets or cash flows are transferred by the originator or an intermediary, typically an investment bank, to a structured entity which issues securities to investors. Asset securitisations involve issuing debt securities (asset-backed securities) that are backed by the cash flows of income-generating assets (ranging from credit card receivables to residential mortgage loans).

Settlement balances - payables and receivables that result from purchases and sales of financial instruments recognised on trade date. Asset settlement balances are amounts owed to the Group in respect of sales and liability settlement balances are amounts owed by the Group in respect of purchases.

Sovereign exposures - exposures to governments, ministries, departments of governments and central banks.

Standardised approach - a method used to calculate credit risk capital requirements under Pillar 1. In this approach the risk weights used in the capital calculation are determined by regulators. For operational risk, capital requirements are determined by multiplying three years' historical gross income by a percentage determined by the regulator. The percentage ranges from 12 to 18%, depending on the type of underlying business being considered.

Standstill - is an agreement, usually for a specified period of time, not to enforce the lender's rights as a result of a customer breaching the terms and conditions of their facilities. This is a concession to the customer. A standstill is most commonly used in a complex restructuring of a company's debts, where a group of creditors agree to delay enforcement action to give the company time to gather information and formulate a strategy with a view to establishing a formal restructuring.

Stress testing - a technique used to evaluate the potential effects on an institution's financial condition of an exceptional but plausible event and/or movement in a set of financial variables.

Stressed value-at-risk (SVaR) - a VaR measure using historical data from a one year period of stressed market conditions. For the purposes of calculating regulatory SVaR, a time horizon of ten trading days is assumed at a confidence level of 99%. Refer also to Value-at-risk below.

Structured credit portfolio (SCP) - a portfolio of certain illiquid assets - principally CDO super senior positions, negative basis trades and monoline exposures.

Structured entity (SE) - an entity that has been designed such that voting or similar rights are not the dominant factor in deciding who controls the entity, for example when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. SEs are usually established for a specific, limited purpose, they do not carry out a business or trade and typically have no employees. They take a variety of legal forms - trusts, partnerships and companies - and fulfil many different functions.

Structured notes - securities that pay a return linked to the value or level of a specified asset or index. Structured notes can be linked to equities, interest rates, funds, commodities and foreign currency.

Subordinated liabilities - liabilities which, in the event of insolvency or liquidation of the issuer, are subordinated to the claims of depositors and other creditors of the issuer.

Super senior CDO - the most senior class of instrument issued by a CDO vehicle. They benefit from the subordination of all other instruments, including AAA rated securities, issued by the CDO vehicle.

Supervisory slotting approach - a method of calculating regulatory capital, specifically for lending exposures in project finance and income producing real estate, where the PD estimates do not meet the minimum internal ratings based standards. Under this approach, the bank classifies exposures from 1 to 5, where 1 is strong and 5 is default. Specific risk-weights are assigned to each classification.

Tier 1 capital - a component of regulatory capital, comprising Common Equity Tier 1 and Additional Tier 1. Additional Tier 1 capital includes eligible non-common equity capital securities and any related share premium. Under Basel II, Tier 1 capital comprises Core Tier 1 capital plus other Tier 1 securities in issue, less certain regulatory deductions.

Tier 2 capital - qualifying subordinated debt and other Tier 2 securities in issue, eligible collective impairment allowances less certain regulatory deductions.

Total loss absorbing capacity (TLAC) - a Financial Stability Board requirement for global systemically important banks to have a sufficient amount of specific types of liabilities which can be used to absorb losses and recapitalise a bank in resolution. The implementation of the TLAC requirements is being discussed within local regulators.

Glossary of terms

Unaudited - financial information that has not been subjected to the audit procedures undertaken by the Group's auditors to enable them to express an opinion on the Group's financial statements.

US Federal Agencies - are independent bodies established by the US Government for specific purposes such as the management of natural resources, financial oversight or national security. A number of agencies, including, the Government National Mortgage Association, issue or guarantee publicly traded debt securities.

Value-at-risk (VaR) - a technique that produces estimates of the potential loss in the market value of a portfolio over a specified time period at a given confidence level.

Wholesale funding - wholesale funding comprises Deposits by banks, Debt securities in issue and Subordinated liabilities.

Write-down - a reduction in the carrying value of an asset to record a decline in its fair value or value in use.

Wrong-way risk - the risk of loss when the risk factors driving the exposure to a counterparty or customer are positively correlated with the creditworthiness of that counterparty i.e. the size of the exposure increases at the same time as the risk of the counterparty or customer being unable to meet that obligation, increases.

Forward looking statements

Certain sections in this document contain 'forward-looking statements' as that term is defined in the United States Private Securities Litigation Reform Act of 1995, such as statements that include the words 'expect', 'estimate', 'project', 'anticipate', 'believe', 'should', 'intend', 'plan', 'could', 'probability', 'risk', 'Value-at-Risk (VaR)', 'target', 'goal', 'objective', 'may', 'endeavour', 'outlook', 'optimistic', 'prospects' and similar expressions or variations on these expressions.

In particular, this document includes forward-looking statements relating, but not limited to: RBSG and the Group's restructuring, which includes the separation and divestment of Williams & Glyn, the proposed restructuring of RBSG's CIB business, the implementation of the UK ring-fencing regime, the implementation of a major development program to update RBSG and the Group's IT infrastructure and the continuation of its balance sheet reduction programme, as well as capital and strategic plans, divestments, capitalisation, portfolios, net interest margin, capital and leverage ratios and requirements liquidity, risk-weighted assets (RWAs), RWA equivalents (RWAe), Pillar 2A, return on equity (ROE), profitability, cost:income ratios, loan:deposit ratios, AT1 and other funding plans, funding and credit risk profile; litigation, government and regulatory investigations; RBSG and the Group's future financial performance; the level and extent of future impairments and write-downs; including with respect to Goodwill; future pension contributions and RBSG and the Group's exposure to political risks, operational risk, conduct risk and credit rating risk and to various types of market risks, such as interest rate risk, foreign exchange rate risk and commodity and equity price risk. These statements are based on current plans, estimates, targets and projections, and are subject to inherent risks, uncertainties and other factors which could cause actual results to differ materially from the future results expressed or implied by such forward-looking statements. For example, certain market risk disclosures are dependent on choices relying on key model characteristics and assumptions and are subject to various limitations. By their nature, certain of the market risk disclosures are only estimates and, as a result, actual future gains and losses could differ materially from those that have been estimated.

Other factors that could adversely affect our results and the accuracy of forward-looking statements in this document include the risk factors and other uncertainties discussed in this document. These include the significant risks for RBSG and the Group presented by the outcomes of the legal, regulatory and governmental actions and investigations that RBSG is subject to (including active civil and criminal investigations) and any resulting material adverse effect on RBSG of unfavourable outcomes (including where resolved by settlement); the uncertainty relating to the referendum on the UK's membership of the European Union and the consequences of it; the separation and divestment of Williams & Glyn; RBSG and the Group's ability to successfully implement the various initiatives that are comprised in its restructuring plan, particularly the proposed restructuring of its CIB business and the balance sheet reduction programme as well as the significant restructuring required to be undertaken by RBSG and the Group in order to implement the UK ring fencing regime; the significant changes, complexity and costs relating to the implementation of its restructuring, the separation and divestment of Williams & Glyn and the UK ring-fencing regime; whether the Group will emerge from its restructuring and the UK ring-fencing regime as a viable, competitive, customer focused and profitable bank; RBSG's ability to achieve its capital and leverage requirements or targets which will depend on RBSG and the Group's success in reducing the size of its business and future profitability; ineffective management of capital or changes to regulatory requirements relating to capital adequacy and liquidity or failure to pass mandatory stress tests; the ability to access sufficient sources of capital, liquidity and funding when required; changes in the credit ratings of RBSG, the Bank or the UK government; declining revenues resulting from lower customer retention and revenue generation in light of RBSG and the Group 's strategic refocus on the UK the impact of global economic and financial market conditions (including low or negative interest rates) as well as increasing competition.

In addition, there are other risks and uncertainties. These include operational risks that are inherent to the Group's business and will increase as a result of the Group's significant restructuring; the potential negative impact on the Group's business of actual or perceived global economic and financial market conditions and other global risks; the impact of unanticipated turbulence in interest rates, yield curves, foreign currency exchange rates, credit spreads, bond prices, commodity prices, equity prices; basis, volatility and correlation risks; heightened regulatory and governmental scrutiny and the increasingly regulated environment in which RBSG and The Group operate; the risk of failure to realise the benefit of the Group's substantial investments in its information technology and systems, the risk of failing to prevent a failure of RBSG or the Group's IT systems or to protect itself and its customers against cyber threats, reputational risks; risks relating to the failure to embed and maintain a robust conduct and risk culture across the organisation or if its risk management framework is ineffective; risks relating to increased pension liabilities and the impact of pension risk on RBSG and the Group's capital position; increased competitive pressures resulting from new incumbents and disruptive technologies; the Group's ability to attract and retain qualified personnel; HM Treasury exercising influence over the operations of RBSG; limitations on, or additional requirements imposed on, the Group's activities as a result of HM Treasury's investment in RBSG; the extent of future write-downs and impairment charges caused by depressed asset valuations; deteriorations in borrower and counterparty credit quality; the value and effectiveness of any credit protection purchased by the Group; risks relating to the reliance on valuation, capital and stress test models and any inaccuracies resulting therefrom or failure to accurately reflect changes in the micro and macroeconomic environment in which the Group operates, risks relating to changes in applicable accounting policies or rules which may impact the preparation of the Group's financial statements; the impact of the recovery and resolution framework and other prudential rules to which the Group is subject, the recoverability of deferred tax assets by the Group; and the success of RBSG and the Group in managing the risks involved in the foregoing.

The forward-looking statements contained in this document speak only as at the date hereof, and the Group does not assume or undertake any obligation or responsibility to update any forward-looking statement to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

The information, statements and opinions contained in this document do not constitute a public offer under any applicable legislation or an offer to sell or solicit of any offer to buy any securities or financial instruments or any advice or recommendation with respect to such securities or other financial instruments.

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