Registered Number: 25766

ULSTER BANK IRELAND LIMITED

REPORT OF DIRECTORS AND FINANCIAL STATEMENTS

31 December 2012

ULSTER BANK IRELAND LIMITED

CONTENTS

ULSTER BANK IRELAND LIMITED

BOARD OF DIRECTORS AND SECRETARIES

Directors	S Bell (Executive Director) J Brown (Executive Director) S Dorgan (Chairman and Independent Non-Executive Director) E Gleeson (Independent Non-Executive Director) P Nolan (Independent Non-Executive Director) D O'Shea (Independent Non-Executive Director) B Rosewell (Independent Non-Executive Director)
Registered Office	Ulster Bank Group Centre George's Quay Dublin 2
Secretaries	R Curran E Dignam (Deputy Secretary)
Auditors	Deloitte & Touche Chartered Accountants & Statutory Audit Firm Deloitte and Touche House Earlsfort Terrace Dublin 2

ULSTER BANK IRELAND LIMITED

REPORT OF THE DIRECTORS

The directors of Ulster Bank Ireland Limited ("the Bank") present their report, together with audited financial statements of the Bank and its subsidiaries (together "the Group") for the year ended 31 December 2012. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union (EU).

ACTIVITIES AND BUSINESS REVIEW

Principal activities

The Bank is a leading retail and commercial bank in the Republic of Ireland. It provides a comprehensive range of financial services through both its Retail Banking division, which provides loan and deposit products through a network of branches and direct channels and its Corporate Banking division, which provides services to business and corporate customers.

Business review

The Group's performance continues to be impacted by difficult economic conditions in the Republic of Ireland and a challenging macroeconomic environment, including continued uncertainty arising from concerns regarding the future economic outlook in the Eurozone.

The Group's financial performance reflects this with charges for bad and non performing loans continuing to have a significant negative impact, although to a lesser extent than in previous years. The market for deposits remains competitive and margins continue to be constrained, however the Group has, nonetheless, increased external customer deposits by in excess of €1bn in the year to 31 December 2012.

The directors continue to implement a strategy to strengthen its underlying business, support its customers and return the Group to sustainable profitability. In its ambition to become the compelling choice for banking on the island of Ireland, the Group has continued to implement a number of actions to simplify its operating model, to better serve its customers, reduce operating costs across the Group and continue to build on commitments made to its customers through its 'Helpful Banking' campaign.

In June 2012 a significant number of the Group's customers were impacted by The Royal Bank of Scotland Group plc ("RBS Group") technology incident affecting the Bank's transaction batch processing. Throughout the incident the Bank took action to help customers experiencing difficulty by opening branches for longer and increasing the number of staff in locally based call centres. Thereafter the Bank focused on honouring its commitment to put impacted customers back to the position they would have been in had the incident not occurred. Staff, customer redress and other costs associated with the incident amounted to €59m.

Financial performance

The Group's financial performance is presented in the Consolidated Income Statement on page 8.

Net interest income decreased by 11% due to the impact of higher funding costs coupled with a reduction in the loan book and an increase in non-performing loans.

Non-interest income decreased from €422m to €252m, primarily due to the 2011 gain on the buy-back of certain externally issued mortgage securitisation bonds at a discount to par.

Operating expenses increased by 11% on prior year as underlying cost savings were negated by costs of €59m associated with the RBS Group technology incident.

Impairment losses have decreased from €3,413m to €2,437m but remain at a heightened level due to ongoing challenging economic conditions.

At the end of the year the total assets of the Group were €40,912m (2011: €44,636m).

Risk management

The Group's future performance and results could be materially different from expected results depending on the outcome of certain potential risks and uncertainties.

The major risks associated with the Group's businesses are credit, liquidity, market, regulatory, reputational, conduct, operational and sovereign risk. The Group has established a comprehensive framework for managing these risks, which is continually evolving as the Group's business activities change in response to market, credit, product, regulatory and other developments. The Group is also exposed to risks from its defined benefit pension scheme. The Group's policies for managing each of these risks and its exposure thereto are detailed in Note 23 to the financial statements.

Business review (continued)

Accounting policies

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Details of the Group's critical accounting policies and key sources of accounting judgements are included in the Accounting Policies on pages 21 to 23.

Outlook

The directors acknowledge the challenges of the external market and customer environment. They consider the Group and Bank to be in a stable financial position and confirm that it has adequate resources, with ongoing support from RBS Group, to continue in business for the foreseeable future.

Share capital

Details of the share capital can be found in Note 20 to the financial statements.

Directors and secretaries

The names of the current members of the Board of Directors are shown on page 1. From 1 January 2012 to date the following changes have taken place:

Directors	Appointed	Resigned
B Rosewell	11 January 2012	
S Bell	23 March 2012	
D O'Shea	12 November 2012	
C McManus		12 November 2012
Deputy Secretary		
E Dignam	1 January 2012	

In accordance with the Articles of Association, the directors are not required to retire by rotation.

Interests of directors and secretaries

At 31 December 2012 the directors and secretaries of the Bank had no beneficial interests in the shares or debentures of RBS Group companies other than that disclosed in Note 32 to the financial statements.

Books of account

The measures taken by the directors to ensure compliance with the Bank's obligation to keep proper books of account, under Section 202 of the Companies Act 1990, are the use of appropriate systems and procedures and employment of competent persons. The books of account are kept at the offices of the Bank at Ulster Bank Group Centre, George's Quay, Dublin 2 and Ulster Bank Group Head Office, Donegall Square East, Belfast, BT1 5UB.

Staff involvement

The Group values the input of its employees and actively seeks opportunities to engage with staff at all levels. The annual survey of employee opinions known as Your Feedback provides valuable data to decision makers across the Group in support of improving employee engagement and satisfaction.

Employees across the Group continued to give generously, both financially and through volunteering, to many community and other worthy causes. Such giving is encouraged by the Group through its use of matched funding and staff charity funds which support worthy causes at local, national and international level.

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

Employment of disabled persons

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

Diversity

The delivery of an effective equal opportunities policy is a natural and integral part of good management practice. A key element of the Group's policy is to ensure staff know about development opportunities and are encouraged to develop to their full potential. It is the Group's policy to comply with the relevant provisions of legislation and have regard to Codes of Practice affecting employment practices.

The Group's commitment to diversity underpins its desire to be the financial services provider of choice for its customers and to be the employer of choice for its people. The Group will recruit, retain, develop and promote people based solely on merit regardless of their gender, disability, political opinion, race, religious belief or any other characteristics.

Safety, health and wellbeing

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

During 2012, the Group continued to focus on compliance, governance and managing risks across the Group. Opportunities to improve the efficiency and effectiveness of safety, health and wellbeing management policies and services were monitored and, where relevant, implemented.

Policy and practice on payment of creditors

The Group is committed to maintaining a normal commercial relationship with its suppliers. Consequently, it is the Group's policy to negotiate and agree terms and conditions with its suppliers, which includes the giving of an undertaking to pay suppliers within 30 days of receipt of a correctly prepared invoice submitted in accordance with the terms of the contract or such other payment period as may be agreed.

RBS Group Payables manages the creditors payments process on behalf of various RBS Group entities, including Ulster Bank Ireland Limited and its subsidiaries. At 31 December 2012, the amount owed to trade creditors by the RBS Group, expressed as a proportion of the amounts invoiced by suppliers during the year then ended, was 25 days (2011: 27 days).

Charitable contributions

During the year the Group made charitable and community investment donations in the Republic of Ireland totalling €515,167 (2011: €594,985).

Political donations

During the year the Group did not make any political donations (2011: €nil).

Branches outside the Republic of Ireland

The Bank has a branch, within the meaning of European Communities (Credit Institutions: Accounts) Regulations, 1992, in Northern Ireland.

Compliance with the Corporate Governance Code for Credit Institutions and Insurance Undertakings

The Corporate Governance Code for Credit Institutions and Insurance Undertakings ("the Code") imposes minimum core standards upon all credit institutions and insurance undertakings with additional requirements upon entities which are designated as major institutions. The Bank has been designated as a major institution and is therefore subject to the requirements for major institutions included within Appendix 1 of the Code.

ULSTER BANK IRELAND LIMITED

<u>REPORT OF THE DIRECTORS</u> (continued)

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position, including potential risks and uncertainties, are set out in the Business review on pages 2 and 3.

The financial position of the Group, its cash flows, liquidity position, capital and funding sources are set out in the financial statements. Notes 23 and 24 to the financial statements include the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to market, credit and liquidity risk.

The Group is part of the RBS Group and receives ongoing capital, funding and liquidity resources which, coupled with other sources of funding and liquidity, enable the Group to meet its obligations as they fall due. Other sources of funding and liquidity include retail, wholesale and central bank liquidity facilities.

The directors are satisfied that the Group will continue to receive support from the RBS Group by way of capital, funding and liquidity facilities. After considering the Group's financial outlook and related funding and capital needs, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Investments in Group undertakings

The investments in Group undertakings are shown in Note 12. All of these companies are included in the Group's consolidated financial statements and all have an accounting reference date of 31 December.

Dividends

The directors do not recommend the payment of a dividend (2011: €nil).

Post balance sheet events

There have been no significant events between the year end and the date of approval of the financial statements which would require a change or additional disclosure or amendment in the financial statements.

Auditors

The auditors, Deloitte & Touche, Chartered Accountants and Statutory Audit Firm, will continue in office in accordance with Section 160(2) of the Companies Act 1963.

Signed on behalf of the Board:

Stephen Bell Chief Risk Officer	James Brown Group Chief Executive	Sean Dorgan Chairman

22 February 2013

ULSTER BANK IRELAND LIMITED

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Irish company law requires the directors to prepare the Group and Bank's financial statements for each financial year which give a true and fair view of the state of affairs of the Group and Bank and of the profit or loss of the Group and Bank for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies for the Group and Bank's financial statements and then apply them consistently;

- make judgements and estimates that are reasonable and prudent; and

- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Bank will continue in business.

The directors are responsible for keeping proper books of account which disclose with reasonable accuracy at any time the financial position of the Group and Bank and to enable them to ensure that the financial statements are prepared in accordance with IFRS as adopted by the EU and comply with Irish statute comprising the Companies Acts, 1963 to 2012 and European Communities (Credit Institutions: Accounts) Regulations, 1992. They are also responsible for safeguarding the assets of the Group and Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Signed on behalf of the Board:

Stephen Bell Chief Risk Officer	James Brown Group Chief Executive	Sean Dorgan Chairman

22 February 2013

ULSTER BANK IRELAND LIMITED

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF ULSTER BANK IRELAND LIMITED

We have audited the financial statements of Ulster Bank Ireland Limited ("the Bank") and its subsidiaries (together "the Group") for the year ended 31 December 2012 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Balance Sheets, the Statements of Changes in Equity, the Cash Flow Statements, the accounting policies and the related notes 1 to 35. The financial reporting framework that has been applied in their preparation is Irish law and International Financial Reporting Standards (IFRS) as adopted by the European Union.

This report is made solely to the Bank's members, as a body, in accordance with Section 193 of the Companies Act, 1990. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' 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 auditors
As explained more fully in the Statement of Directors' Responsibilities, the directors are responsible for the preparation of the financial statements giving a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with Irish 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 company'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 Report of the Directors and Financial Statements for the year ended 31 December 2012 to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion
In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the affairs of the Group as at 31 December 2012 and of its loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Acts, 1963 to 2012 and the European Communities (Credit Institutions: Accounts) Regulations, 1992;
- the Bank's financial statements give a true and fair view, in accordance with IFRSs, as adopted by the European Union, of the state of affairs of the Bank as at 31 December 2012; and
- the Bank's financial statements have been properly prepared in accordance with the Companies Acts, 1963 to 2012 and the European Communities (Credit Institutions: Accounts) Regulations, 1992.

Matters on which we are required to report by the Companies Acts 1963 to 2012

- We have obtained all the information and explanations which we consider necessary for the purposes of our audit.
- In our opinion proper books of account have been kept by the Bank.
- The Bank's balance sheet is in agreement with the books of account.
- In our opinion the information given in the Report of the Directors is consistent with the financial statements.
- The net assets of the Bank, as stated in the balance sheet are more than half of the amount of its called-up share capital and, in our opinion, on that basis there did not exist at 31 December 2012 a financial situation which under Section 40(1) of the Companies (Amendment) Act, 1983 would require the convening on an extraordinary general meeting of the Bank.

Matters on which we are required to report by exception
We have nothing to report in respect of the provisions in the Companies Acts 1963 to 2012 which require us to report to you if, in our opinion, the disclosures of directors' remuneration and transactions specified by law are not made.

Martin Reilly (Senior Statutory Auditor)
For and on behalf of Deloitte & Touche
Chartered Accountants and Statutory Audit Firm
Dublin, Ireland

22 February 2013

ULSTER BANK IRELAND LIMITED

CONSOLIDATED INCOME STATEMENT *for the year ended 31 December 2012*

	Note	**2012 €m**	2011 €m
Interest receivable		**1,230**	1,458
Interest payable		**(596)**	(745)
Net interest income	1	**634**	713
Fees and commission receivable		**109**	92
Fees and commission payable		**(4)**	(4)
Income from trading activities		**119**	23
Other operating income		**28**	311
Non-interest income	2	**252**	422
Total income		**886**	1,135
Operating expenses	3	**(590)**	(533)
Operating profit before impairment losses		**296**	602
Impairment losses on loans and advances	9	**(2,437)**	(3,413)
Operating loss before tax		**(2,141)**	(2,811)
Tax (charge)/credit	6	**(247)**	114
Loss for the year		**(2,388)**	(2,697)
Profit/(loss) attributable to:			
Non-controlling interests		**-**	9
Ordinary shareholders		**(2,388)**	(2,706)
		(2,388)	(2,697)

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 85 form an integral part of these financial statements.

The financial statements were approved by the Board of Directors on 22 February 2013 and signed on its behalf by:

Stephen Bell
Chief Risk Officer

James Brown
Group Chief Executive

Sean Dorgan
Chairman

Rachel Curran
Company Secretary

ULSTER BANK IRELAND LIMITED

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME *for the year ended 31 December 2012*

	2012 €m	2011 €m
Loss for the year	**(2,388)**	(2,697)
Other comprehensive(losses)/income:		
Fair value losses on available-for-sale financial assets	**(1)**	(3)
Exchange differences on translation of foreign operations	**8**	(1)
Actuarial gains on defined benefit plans and other movements	**25**	8
Other comprehensive gain	**32**	4
Total comprehensive loss for the year	**(2,356)**	(2,693)
Attributable to:		
Non-controlling interests	**-**	9
Ordinary shareholders	**(2,356)**	(2,702)
	(2,356)	(2,693)

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 85 form an integral part of these financial statements.

ULSTER BANK IRELAND LIMITED

BALANCE SHEETS *as at 31 December 2012*

		Group		Bank	
	Note	**2012 €m**	2011 €m	**2012 €m**	2011 €m
Assets					
Cash and balances at central banks	8	**221**	272	**221**	272
Loans and advances to banks	8	**4,082**	3,404	**3,013**	2,274
Loans and advances to customers	8	**35,176**	39,013	**37,673**	41,277
Debt securities	8,10	**-**	32	**11,079**	12,580
Equity shares	8,11	**8**	6	**8**	6
Investments in Group undertakings	8,12	**-**	-	**191**	191
Derivatives	8,15	**983**	1,245	**980**	1,125
Property, plant and equipment	8,14	**270**	265	**160**	184
Prepayments, accrued income and other assets	8,16	**50**	47	**46**	30
Retirement benefit assets	4,8	**33**	11	**33**	11
Deferred taxation	8,18	**89**	341	**89**	341
Total assets		**40,912**	44,636	**53,493**	58,291
Liabilities					
Deposits by banks	8	**6,272**	12,306	**6,205**	12,319
Customer accounts	8	**19,897**	17,966	**36,912**	36,390
Debt securities in issue	8	**3,989**	4,175	**43**	23
Derivatives	8,15	**1,260**	1,673	**1,076**	1,325
Accruals, deferred income and other liabilities	8,17	**286**	324	**280**	310
Deferred taxation	8,18	**4**	1	**4**	1
Subordinated liabilities	8,19	**956**	946	**956**	946
Total liabilities		**32,664**	37,391	**45,476**	51,314
Equity					
Non-controlling interests		**24**	23	**-**	-
Shareholders' equity:					
Called up share capital	20	**3,592**	3,592	**3,592**	3,592
Reserves		**4,632**	3,630	**4,425**	3,385
Total equity	8	**8,248**	7,245	**8,017**	6,977
Total liabilities and equity		**40,912**	44,636	**53,493**	58,291

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 85 form an integral part of these financial statements.

The financial statements were approved by the Board of Directors on 22 February 2013 and signed on its behalf by:

Stephen Bell Chief Risk Officer	James Brown Group Chief Executive	Sean Dorgan Chairman	Rachel Curran Company Secretary

ULSTER BANK IRELAND LIMITED

STATEMENTS OF CHANGES IN EQUITY *for the year ended 31 December 2012*

	Group		Bank	
	2012	2011	**2012**	2011
	€m	€m	**€m**	€m
Called up share capital				
At 1 January and 31 December	**3,592**	3,592	**3,592**	3,592
Share premium account				
At 1 January and 31 December	**1,142**	1,142	**1,142**	1,142
Available-for-sale reserve				
At 1 January	**1**	4	**1**	4
Unrealised losses in the year	**-**	(3)	**-**	(3)
Realised losses in the year	**(1)**	-	**(1)**	-
At 31 December	**-**	1	**-**	1
Foreign exchange reserve				
At 1 January	**13**	14	**1**	1
Retranslation of net assets	**8**	(1)	**-**	-
At 31 December	**21**	13	**1**	1
Retained earnings				
At 1 January	**(6,653)**	(3,955)	**(6,886)**	(4,056)
Actuarial gains/(losses) on defined benefit plans and other movements	**25**	8	**26**	(1)
Loss attributable to ordinary shareholders	**(2,388)**	(2,706)	**(2,343)**	(2,829)
At 31 December	**(9,016)**	(6,653)	**(9,203)**	(6,886)
Capital contribution				
At 1 January	**9,127**	4,512	**9,127**	4,512
Capital contribution received in the year	**3,358**	4,615	**3,358**	4,615
At 31 December	**12,485**	9,127	**12,485**	9,127
Shareholders' equity at 31 December	**8,224**	7,222	**8,017**	6,977
Non-controlling interests				
At 1 January	**23**	59	**-**	-
Increase/(decrease) in loans classed as equity	**1**	(45)	**-**	-
Profit attributable to non-controlling interests	**-**	9	**-**	-
At 31 December	**24**	23	**-**	-
Total equity at 31 December	**8,248**	7,245	**8,017**	6,977

Total comprehensive loss recognised in the Statement of Changes in Equity is attributable as follows:

Non-controlling interests	**-**	9	**-**	-
Ordinary shareholders	**(2,356)**	(2,702)	**(2,318)**	(2,833)
	(2,356)	(2,693)	**(2,318)**	(2,833)

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 85 form an integral part of these financial statements.

ULSTER BANK IRELAND LIMITED

CASH FLOW STATEMENTS *for the year ended 31 December 2012*

	Note	Group 2012 €m	Group 2011 €m	Bank 2012 €m	Bank 2011 €m
Operating activities					
Operating loss before tax		**(2,141)**	(2,811)	**(2,096)**	(2,945)
Adjustments for:					
Depreciation, amortisation and impairment		**33**	23	**30**	20
Interest on subordinated liabilities		**32**	35	**19**	19
Charge for defined benefit pension schemes		**23**	23	**23**	23
Cash contribution to defined benefit pension schemes		**(45)**	(42)	**(45)**	(42)
Loan impairment provisions net of recoveries		**2,311**	3,235	**2,311**	3,235
Elimination of foreign exchange differences		**14**	32	**8**	34
Other non-cash items		**(224)**	(267)	**(229)**	(292)
Net cash flows from trading activities	26	**3**	228	**21**	52
Changes in operating assets and liabilities		**(2,434)**	(5,664)	**(2,374)**	(6,554)
Net cash flows from operating activities before tax		**(2,431)**	(5,436)	**(2,353)**	(6,502)
Income taxes (paid)/received		**(54)**	40	**(52)**	15
Net cash flows from operating activities	26	**(2,485)**	(5,396)	**(2,405)**	(6,487)
Investing activities					
Sale and maturity of securities		**-**	176	**-**	176
Purchase of equity shares		**(2)**	(4)	**(2)**	(4)
Sale of property, plant and equipment		**1**	9	**2**	1
Purchase of property, plant and equipment		**(8)**	(9)	**(5)**	(5)
Net cash flows from investing activities		**(9)**	172	**(5)**	168
Financing activities					
Capital contribution		**3,358**	4,615	**3,358**	4,615
Interest on subordinated liabilities		**(32)**	(35)	**(19)**	(19)
Net cash flows from financing activities		**3,326**	4,580	**3,339**	4,596
Effect of exchange rate changes on cash and cash equivalents		**23**	2	**21**	2
Net increase/(decrease) in cash and cash equivalents		**855**	(642)	**950**	(1,721)
Cash and cash equivalents 1 January	29	**3,270**	3,912	**2,117**	3,838
Cash and cash equivalents 31 December	29	**4,125**	3,270	**3,067**	2,117

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 85 form an integral part of these financial statements.

ULSTER BANK IRELAND LIMITED

ACCOUNTING POLICIES

1. Presentation of financial statements

The consolidated financial statements are prepared on a going concern basis and in accordance with IFRS issued by the International Accounting Standards Board (IASB), and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB as adopted by the EU. The Group and Bank's financial statements are presented in accordance with the Companies Acts 1963 to 2012 and the European Communities (Credit Institutions: Accounts) Regulations, 1992.

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

2. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and entities (including certain special purpose entities) that are controlled by the Bank (its subsidiaries). Control exists where the Group has the power to govern the financial and operating policies of the entity so as to obtain benefit from its activities; generally conferred by holding a majority of voting rights.

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

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

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

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 at fair value through profit or loss is determined using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or liabilities) and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. Calculation of the effective interest rate takes into account fees payable or receivable, that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual terms of a financial instrument are considered when estimating future cash flows.

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

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 through profit or loss over the life of the facility otherwise they are deferred and included in the effective interest rate on the advance.

ACCOUNTING POLICIES (continued)

3. Revenue recognition (continued)

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

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

Card related services: fees from credit card business include:

- Commission received from retailers for processing credit and debit card transactions: income is accrued to the income statement as the service is performed;
- Interchange received: as issuer, the Group receives a fee (interchange) each time a cardholder purchases goods and services. The Group also receives interchange fees from other card issuers for providing cash advances through its branch and automated teller machine networks. These fees are accrued once the transaction has taken place; and
- Annual fees payable by credit card holders: these are deferred and taken to profit or loss over the period of the service i.e. 12 months.

Insurance brokerage: this is made up of fees and commissions received from the agency sale of insurance. Commission on the sale of an insurance contract is earned at the inception of the policy as the insurance has been arranged and placed. However, provision is made where commission is refundable in the event of policy cancellation in line with estimated cancellations.

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

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

4. Pensions and other post-retirement benefits

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

For defined benefit schemes, scheme liabilities are measured on an actuarial basis using the projected unit credit method and discounted at a rate that reflects the current rate of return on a high quality corporate bond of equivalent term and currency to the scheme liabilities. Scheme assets are measured at their fair value. Cumulative actuarial gains or losses that exceed 10 percent of the greater of the assets or the obligations of the scheme are amortised to the statement of comprehensive income over the expected average remaining lives of participating employees. Past service costs are recognised immediately to the extent that benefits have vested; otherwise they are amortised over the period until the benefits become vested.

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

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

5. Intangible assets and goodwill

Intangible assets that are acquired by the Group are stated at cost less accumulated amortisation and accumulated impairment losses. The intangible assets of the Group and Bank are fully impaired.

ACCOUNTING POLICIES (continued)

6. Property, plant and equipment

Items of property, plant and equipment (except investment properties – see accounting policy 8) are stated at cost less accumulated depreciation (see below) and accumulated impairment losses. Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for separately.

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

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

The residual value and useful life of property, plant and equipment are reviewed at each balance sheet date and updated for any changes.

7. Impairment of intangible assets and property, plant and equipment

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

8. Investment properties

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

Fair value of the investment properties is determined on at least an annual basis by officers of the Group. A selection of properties may be valued by external appointed surveyors from time to time as the commercial need arises. Gains and losses arising from changes in the fair value of investment property are included in profit or loss in the period in which they arise.

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

ACCOUNTING POLICIES (continued)

9. Foreign currencies

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

Transactions in foreign currencies are translated into Euro at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into Euro at the rates of exchange ruling at the balance sheet date. Foreign exchange differences arising on translation are reported in income from trading activities except for differences arising on cash flow hedges and hedges of net investments in foreign operations. Non-monetary items denominated in foreign currencies that are stated at fair value are translated into Euro at foreign exchange rates ruling at the dates the values were 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 included in the available-for-sale reserve in equity unless the asset is the hedged item in a fair value hedge.

Assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into Euro at foreign exchange rates ruling at the balance sheet date. Income and expenses of foreign operations are translated into Euro at average exchange rates unless these do not approximate to the foreign exchange rates ruling at the dates of the transactions. Foreign exchange differences arising on translation of foreign operations are recognised directly in equity and included in profit or loss on its disposal.

10. 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. Other contracts to lease assets are classified as operating leases.

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

Rental income from operating leases is credited to the income statement on a receivable basis over the term of the lease. Operating lease assets are included within property, plant and equipment and depreciated over their useful lives (see accounting policy 6). Operating lease rentals receivable are included in other operating income.

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

11. Provisions and contingent liabilities

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

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 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 obligations under it exceed the expected economic benefits. When the Group vacates a leasehold property, a provision is recognised for the costs under the lease less any expected economic benefits (such as rental income).

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

12. Taxation

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

12. Taxation (continued)

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

Deferred tax is the tax expected to be payable or recoverable in respect of temporary differences between the carrying amount of an asset or liability for accounting purposes and its carrying amount for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that they will be recovered. Deferred tax is 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.

13. Financial assets

On initial recognition financial assets are classified into held-to-maturity investments; available-for-sale financial assets; held for-trading; designated as at fair value through profit or loss; or loans and receivables.

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

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

The Group has designated financial assets as at fair value through profit or loss principally where the assets are economically hedged by derivatives and fair value designation eliminates the measurement inconsistency that would arise if the assets were carried at amortised cost or classified as available-for-sale.

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 that are not classified as held-to-maturity; held-for-trading; designated as at fair value through profit or loss; or loans and receivables are classified as available-for-sale. Financial assets can be designated as available-for-sale on initial recognition. Available-for-sale financial assets are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at fair value. Unquoted equity investments whose fair value cannot be measured reliably are carried at cost and classified as available-for-sale financial assets. Impairment losses and exchange differences resulting from retranslating the amortised cost of monetary available-for-sale financial assets denominated in a foreign currency are recognised in profit or loss together with interest calculated using the effective interest method (see accounting policy 3). Other changes in the fair value of available-for-sale financial assets and any related tax are reported in a separate component of shareholders' equity until disposal, when the cumulative gain or loss is recognised in profit or loss.

Regular way purchases of financial assets classified as loans and receivables are recognised on settlement date; all other regular way purchases are recognised on trade date.

Fair value for a net open position in a financial asset that is quoted in an active market is the current bid price times the number of units of the instrument held. Fair values for financial assets not quoted in an active market are determined using appropriate valuation techniques including discounting future cash flows, option pricing models and other methods that are consistent with accepted economic methodologies for pricing financial assets.

14. 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, available-for-sale or loans and receivables is impaired. A financial asset or portfolio 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 original effective interest rate of the instrument at initial recognition. For collateralised loans and receivables, estimated future cash flows include cash flows that may result from foreclosure less the costs of obtaining and selling the collateral, whether or not foreclosure is probable.

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

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

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

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

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 equity and there is objective evidence that the asset is impaired, the cumulative loss is removed from equity and recognised in profit or loss. The loss is measured as the difference between the acquisition cost 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.

15. Financial liabilities

On initial recognition financial liabilities are classified into held-for-trading; designated as at fair value through profit or loss; or amortised cost.

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

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

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

The principal category of financial liabilities designated as at fair value through profit or loss is 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 for a net open position in a financial liability that is quoted in an active market is the current offer price times the number of units of the instrument held or issued. Fair values for financial liabilities not quoted in an active market are determined using appropriate valuation techniques including discounting future cash flows, option pricing models and other methods that are consistent with accepted economic methodologies for pricing financial liabilities. Credit valuation adjustments are made when valuing financial liabilities to reflect the Group's own credit rating.

16. Derecognition

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

A financial liability is removed from the balance sheet when the obligation is discharged, or cancelled, or expires. On the redemption or settlement of debt securities (including subordinated liabilities) issued by the Group, the Group derecognises the debt instrument and records a gain or loss being the difference between the debt's carrying amount and the cost of redemption or settlement. The same treatment applies where the debt is exchanged for a new debt issue that has terms substantially different from those of the existing debt. The assessment of whether the terms of the new debt instrument are substantially different takes into account qualitative and quantitative characteristics including a comparison of the discounted present value of the cash flows under the new terms with the discounted present value of the remaining cash flows of the original debt issue.

17. Sale and repurchase transactions

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

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

18. Netting

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

19. Capital instruments

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

20. Derivatives and hedging

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

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

Gains and losses arising from changes in fair value of a derivative are recognised as they arise in non interest income within profit or loss.

21. Share-based payments

The Royal Bank of Scotland Group plc awards options over shares to its employees under various share option schemes. IFRS 2 'Share-based Payment' is applied by The Royal Bank of Scotland Group plc to grants made under these schemes after 7 November 2002 that had not vested on 1 January 2010. The Royal Bank of Scotland Group plc recognises an expense for these transactions with its employees based on the fair value on the date the options are granted. It includes the cost of these awards in determining any recharges of employee costs it makes to subsidiaries in the Group.

22. Cash and cash equivalents

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

23. Shares in Group entities

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

ACCOUNTING POLICIES (continued)

Critical accounting policies and key sources of accounting judgements

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

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

Loan impairment provisions

The Group's loan impairment provisions are established to recognise incurred impairment losses in its portfolio of loans classified as loans and receivables and carried at amortised cost. A loan is impaired when there is objective evidence that events since the loan was granted have affected expected cash flows from the loan. 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.

At 31 December 2012, gross loans and advances to customers totalled €45,891m (2011: €47,647m) and customer loan impairment provisions amounted to €10,715m (2011: €8,634m).

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

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

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

Latent component – this consists of loan losses that have been incurred but have not been separately identified at the balance sheet date. 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 that 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.

Forbearance

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

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

Critical accounting policies and key sources of accounting judgements (continued)

Deferred tax

The Group makes provision for deferred tax on short-term and other temporary differences where tax recognition occurs at a different time from accounting recognition. Deferred tax assets of €89m were recognised as at 31 December 2012 (2011: €341m).

The Group has recognised deferred tax assets in respect of losses. Deferred tax assets are recognised in respect of unused tax losses to the extent that it is probable that there will be future taxable profits against which the losses can be utilised. Business projections prepared for impairment reviews indicate that sufficient future taxable income will be available against which to offset these recognised deferred tax assets within 7 years (2011: 7 years). The Group's cumulative losses are principally attributable to the recent unparalleled market conditions.

Deferred tax assets of €1,087m (2011: €591m) have not been recognised in respect of tax losses carried forward where doubt exists over the availability of future taxable profits.

Pensions

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

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

Any recognisable surplus or deficit in excess of 10% of the greater of scheme assets and scheme liabilities is recognised in the balance sheet as an asset (surplus) or liability (deficit).

In determining the value of scheme liabilities, financial and demographic assumptions are made as to price inflation, pension increases, earnings growth and employee life expectancy. A range of assumptions could be adopted in valuing the schemes' liabilities. Different assumptions could significantly alter the amount of the surplus or deficit recognised in the balance sheet and the pension cost charged to the income statement. The assumptions adopted for the Group's pension schemes are set out in Note 4 to the financial statements together with sensitivities of the balance sheet and income statement to changes in those assumptions. The Group pension gain recognised on the balance sheet at 31 December 2012 was €33m (2011: surplus €11m).

The Group has reduced the allowance made for future discretionary increases to pensions in payment, in light of recent experience.

IAS19 revised
The Group will apply IAS 19 'Employee Benefits revised' (IAS 19 revised) from 1 January 2013. The revised standard requires: the immediate recognition of all actuarial gains and losses eliminating the "corridor approach"; interest cost to be calculated on the net pension liability or asset at the long-term bond rate, an expected rate of return will no longer be applied to assets; and all past service costs to be recognised immediately when a scheme is curtailed or amended. If the Group had adopted IAS 19 revised as at 31 December 2012, the net pension asset would become a net pension liability of €262m (2011: liability of €43m). The loss after tax for the period ended 31 December 2012 would have been lower by €3m (2011 - higher by €2m).

Critical accounting policies and key sources of accounting judgements (continued)

Fair value - financial instruments

Financial instruments classified as held-for-trading or designated as at fair value through profit or loss and financial assets classified as available-for-sale are recognised in the financial statements at fair value. All derivatives are measured at fair value. On the balance sheet, financial assets carried at fair value are included within Debt securities, Equity shares, and Derivatives as appropriate. Financial liabilities carried at fair value are included within Deposits by banks, Customer accounts and Derivatives. Derivative assets and Derivative liabilities are shown separately on the face of the balance sheets. Gains or losses arising from changes in fair value of financial instruments classified as held-for-trading or designated as at fair value through profit or loss are included in the income statement. Unrealised gains and losses on available-for-sale financial assets are recognised directly in equity unless an impairment loss is recognised. The carrying value of a financial asset or a financial liability carried at cost or amortised cost that is the hedged item in a qualifying hedge relationship is adjusted by the gain or loss attributable to the hedged risk.

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

The Group's derivative products include swaps, forwards, futures and options. Exchange traded instruments are valued using quoted prices. The fair value of over-the-counter instruments is derived from pricing models which take account of contract terms, including maturity, as well as quoted market parameters such as interest rates and volatilities. Most of the Group's pricing models do not entail material subjectivity because the methodologies utilised do not incorporate significant judgement and the parameters included in the models can be calibrated to actively quoted market prices. Values established from pricing models are adjusted for credit risk, liquidity risk and future operational costs.

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

More details about the Group's valuation methodologies of the fair value of financial instruments valued using techniques where at least one significant input is unobservable are given in Note 8.

Impairment of investment in Group undertakings

The fair value of investments in Group undertakings is calculated using a model based on expected future profits plus future equity requirements. The net equity flows are discounted relative to the number of years from the current year. A discounted terminal value is added to the discounted expected future profits to provide the fair value of the subsidiary. If the fair value of the subsidiary 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.

Valuation of investment property

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

Fair value of the investment properties is determined on at least an annual basis by officers of the Group. A selection of properties may be valued by external appointed surveyors from time to time as the commercial need arises. Gains and losses arising from changes in the fair value of investment property are included in profit or loss in the period in which they arise.

Accounting developments

The following IFRSs and amendments to IFRS have an effective date of 1 January 2013 except for the Amendments to IAS 1 which have an effective date of 1 July 2012:

IFRS 10 'Consolidated Financial Statements' replaces SIC-12 'Consolidation - Special Purpose Entities' and the consolidation elements of the existing IAS 27 'Consolidated and Separate Financial Statements'. IFRS 10 adopts a single definition of control: a reporting entity controls another entity when the reporting entity has the power to direct the activities of that other entity to generate returns for the reporting entity. IFRS 10 requires retrospective application. Implementation of IFRS 10 will not have a material effect on the Group's financial statements.

IFRS 11 'Joint Arrangements', which supersedes IAS 31' Interests in Joint Ventures', distinguishes between joint operations and joint ventures. Joint operations are accounted for by the investor recognising its assets and liabilities including its share of any assets held and liabilities incurred jointly and its share of revenues and costs. Joint ventures are accounted for in the investor's consolidated accounts using the equity method. IFRS 11 requires retrospective application. Implementation of IFRS 11 will not have a material effect on the Group's financial statements.

IFRS 12 'Disclosure of Interests in Other Entities' covers disclosures for entities reporting under IFRS 10 and IFRS 11 replacing those in IAS 28 and IAS 27. Entities are required to disclose information that helps financial statement readers evaluate the nature, risks and financial effects associated with an entity's interests in subsidiaries, in associates and joint arrangements and in unconsolidated structured entities.

IAS 27 'Separate Financial Statements' comprises those parts of the existing IAS 27 that deal with separate financial statements and IAS 28 'Investments in Associates and Joint Ventures' covers joint ventures as well as associates; both must be accounted for using the equity method. The mechanics of the equity method are unchanged. These two revised standards have no effect on the Group's financial statements.

Although IFRS 10-12 (as amended) and revised IAS 27 and IAS 28 have an effective date of 1 January 2013, they have been endorsed by the EU for application from 1 January 2014. However, early adoption is permitted and the Group implemented these standards from 1 January 2013.

IFRS 13 'Fair Value Measurement' sets out a single IFRS framework for defining and measuring fair value and requiring disclosures about fair value measurements. Implementation of IFRS 13 will not have a material effect on the Group's financial statements.

'Disclosures - Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7)' amended IFRS 7 to require disclosures about the effects and potential effects on an entity's financial position of offsetting financial assets and financial liabilities and related arrangements.

IAS 19 'Employee Benefits' (revised) requires: the immediate recognition of all actuarial gains and losses eliminating the "corridor approach"; interest cost to be calculated on the net pension liability or asset at the long-term bond rate, an expected rate of return will no longer be applied to assets; and all past service costs to be recognised immediately when a scheme is curtailed or amended.

Amendments to IAS 1 'Presentation of Items of Other Comprehensive Income' require items that will never be recognised in profit or loss to be presented separately in other comprehensive income from those items that are subject to subsequent reclassification.

'Annual Improvements 2009-2011 Cycle' makes a number of minor changes to IFRSs. These will not have a material effect on the Group's financial statements.

In October 2012, the IASB issued 'Investment Entities (amendments to IFRS 10, IFRS 12 and IAS 27)'. The amendments apply to 'investment entities': entities whose business is to invest funds solely for returns from capital appreciation, investment income or both and which evaluate the performance of their investments on a fair value basis. The amendments provide an exception to IFRS 10 by requiring investment entities to measure their subsidiaries (other than those that provide services related to the entity's investment activities) at fair value through profit or loss, rather than consolidate them. The amendments are effective from 1 January 2014.

In December 2011, the IASB issued 'Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32)'. The amendments add application guidance to IAS 32 to address inconsistencies identified in applying some of the standard's criteria for offsetting financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after 1 January 2014 and must be applied retrospectively.

Accounting developments (continued)

In November 2009, the IASB issued IFRS 9 'Financial Instruments' simplifying the classification and measurement requirements in IAS 39 in respect of financial assets. The standard reduces the measurement categories for financial assets to two: fair value and amortised cost. A financial asset is classified on the basis of the entity's business model for managing the financial asset and the contractual cash flow characteristics of the financial asset. Only assets with contractual terms that give rise to cash flows on specified dates that are solely payments of principal and interest on principal and which are held within a business model whose objective is to hold assets in order to collect contractual cash flows are classified as amortised cost. All other financial assets are measured at fair value. Changes in the value of financial assets measured at fair value are generally taken to profit or loss.

In October 2010, IFRS 9 was updated to include requirements in respect of the classification and measurement of liabilities. These do not differ markedly from those in IAS 39 except for the treatment of changes in the fair value of financial liabilities that are designated as at fair value through profit or loss attributable to own credit; these must be presented in other comprehensive income.

In December 2011, the IASB issued amendments to IFRS 9 and to IFRS 7 'Financial Instruments: Disclosures' delaying the effective date of IFRS 9 to annual periods beginning on or after 1 January 2015 and introducing revised transitional arrangements including additional transition disclosures. If an entity implements IFRS 9 in 2012 the amendments permit it either to restate comparative periods or to provide the additional disclosures. Additional transition disclosures must be given if implementation takes place after 2012.

IFRS 9 makes major changes to the framework for the classification and measurement of financial instruments and will have a significant effect on the Group's financial statements. The Group is assessing the effect of IFRS 9 which will depend on the results of IASB's reconsideration of IFRS 9's classification and measurement requirements and the outcome of the other phases in the development of IFRS 9.

NOTES TO THE FINANCIAL STATEMENTS *for the year ended 31 December 2012*

1. Net interest income

	Group 2012 €m	Group 2011 €m
Loans and advances to customers	**1,187**	1,391
Loans and advances to banks	**43**	61
Debt securities	**-**	6
Interest receivable	**1,230**	1,458
Customer accounts	**(277)**	(271)
Deposits by banks	**(248)**	(371)
Debt securities in issue	**(39)**	(68)
Subordinated liabilities	**(32)**	(35)
Interest payable	**(596)**	(745)
Net interest income	**634**	713

Included within net interest income is €249m (2011: €233m) of interest on impaired loans.

2. Non-interest income

	Group 2012 €m	Group 2011 €m
Fees and commission receivable	**109**	92
Fees and commission payable	**(4)**	(4)
Income from trading activities [1] :		
Foreign exchange [2]	**19**	26
Interest rates [3]	**100**	(3)
Other operating income:		
Profit on buyback of securitisation bonds	**-**	291
Other income [1]	**28**	20
Non-interest income	**252**	422

The analysis of trading income is based on how the business is organised and the underlying risks managed.

During the year ended 31 December 2011 the Group bought back certain externally issued mortgage securitisation bonds at a discount to par and realised a gain of €291m.

Notes:

Trading income comprises gains and losses on financial instruments held-for-trading, both realised and unrealised, interest income and dividends and the related funding costs. The types of instruments include:

(1) For the year ended 31 December 2011 certain amounts have been reclassified within and between Income from trading activities and Other income to better reflect the underlying nature of the income stream.

(2) Foreign exchange: spot foreign exchange contracts, currency swaps and options, emerging markets and related hedges and funding.

(3) Interest rates: interest rate swaps, forward foreign exchange contracts, forward rate agreements, interest rate options, interest rate futures and related hedges and funding.

ULSTER BANK IRELAND LIMITED

NOTES TO THE FINANCIAL STATEMENTS *for the year ended 31 December 2012*

3. Operating expenses

	Group	
	2012	2011
	€m	€m
Wages, salaries and other staff costs	**220**	214
Social security costs	**25**	22
Pension costs:		
- defined benefit schemes (see Note 4)	**23**	23
- defined contribution schemes (see Note 4)	**3**	2
Restructure costs	**23**	3
Staff costs	**294**	264
Premises and equipment	**86**	112
Administration	**177**	134
Other expenses	**263**	246
Property, plant and equipment depreciation (see Note 14)	**22**	23
Impairment of property, plant and equipment (see Note 14)	**11**	-
Depreciation, amortisation and impairment	**33**	23
	590	533

Included within operating expenses above are the following amounts in respect of costs associated with the technology incident which impacted the Group during 2012:

	2012	2011
	€m	€m
Staff costs	**5**	-
Other expenses	**54**	-
	59	-

The average number of persons employed by the Group during the year, excluding temporary staff was 3,486 (2011: 3,543). The average number of temporary employees during 2012 was 166 (2011: 151). The number of persons employed by the Group at 31 December, excluding temporary staff, was as follows:

	Group	
Employee Numbers	**2012**	2011
	Number	Number
Retail Banking	**1,288**	1,450
Corporate Banking/Other	**2,136**	2,097
	3,424	3,547

	Group	
	2012	2011
Auditors' remuneration	**€'000**	€'000
Statutory audit work	**1,179**	1,091
Non audit work:		
- Other services pursuant to legislation	**-**	10
	1,179	1,101

Other than the amounts disclosed above, no additional remuneration was payable to the auditors for any other services.

4. Pension costs

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

Name of schemes
Ulster Bank Pension Scheme (Republic of Ireland)
First Active Pension Scheme

The schemes were closed to new entrants in 2009, when a new defined contribution scheme was launched.

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

The Group and Bank also makes contributions to a small number of RBS Group Pension Schemes, the costs of which are accounted for as defined contributions.

The Group made contributions of €3,304k to defined contribution schemes in 2012 (2011: €2,148k). The Bank made contributions of €3,304k to defined contribution schemes in 2012 (2011: €2,147k).

The corridor method of accounting permits the Group to defer recognition of actuarial gains and losses that are within 10% of the larger of the fair value of plan assets and the present value of the defined benefits obligations of the scheme on an individual basis at the beginning of the year. Any excess variations are amortised prospectively over the average remaining service lives of current members of the scheme.

The Group will apply IAS 19 'Employee Benefits revised' (IAS 19 revised) from 1 January 2013. The revised standard requires: the immediate recognition of all actuarial gains and losses eliminating the "corridor approach"; interest cost to be calculated on the net pension liability or asset at the long-term bond rate, an expected rate of return will no longer be applied to assets; and all past service costs to be recognised immediately when a scheme is curtailed or amended.

An interim valuation of the scheme was prepared to 31 December 2012 by an independent actuary, using the following assumptions:

	Group and Bank	
Principal actuarial assumptions at 31 December	**2012**	2011
Discount rate	**4.10%**	5.75%
Expected return on plan assets	**4.10%**	5.32% - 5.44%
Rate of increase in salaries	**1.75%**	1.00% - 3.00%
Rate of increase in pensions in payment	**1.50% - 2.00%**	1.50% - 2.00%
Inflation assumption	**2.00%**	2.00%

	Group and Bank	
Major classes of plan assets as a percentage of total plan assets	**2012**	2011
Equities	**45%**	44%
Index-linked bonds	**6%**	13%
Government fixed interest bonds	**2%**	5%
Corporate and other bonds	**19%**	16%
Hedge funds	**11%**	7%
Property	**4%**	5%
Derivatives	**1%**	-
Cash and other assets	**12%**	10%

The disclosures for the period ending on 31 December 2013 will be prepared under IAS19 revised which uses the discount rate rather than best-estimate asset returns to calculate the asset return component of the P&L charge. Therefore a table of expected returns for the current year has not been prepared.

4. Pension costs (continued)

	Group and Bank	
Post-retirement mortality assumptions (Main scheme)	**2012**	**2011**
Longevity at age 70 for current pensioners (years)		
Males	**17.3**	17.1
Females	**18.7**	18.6
Longevity at age 63 for future pensioners (years)		
Males	**23.9**	23.7
Females	**25.5**	25.4

These post-retirement mortality assumptions are derived from standard mortality tables used by the scheme actuary.

	Group and Bank		
Changes in value of net pension asset/(liability)	**Fair value of plan assets €m**	**Present value of defined benefit obligations €m**	**Net pension asset/(liability) €m**
At 1 January 2012	723	(766)	(43)
Income statement:			
Expected return	39	-	39
Interest cost	-	(44)	(44)
Current service cost	-	(21)	(21)
Past service cost	-	3	3
	39	(62)	(23)
Statement of comprehensive income:			
Actuarial gain/(loss)	44	(285)	(241)
Contributions by employer	45	-	45
Contributions by plan participants	3	(3)	-
Benefits paid	(23)	23	-
At 31 December 2012	831	(1,093)	(262)
Unrecognised actuarial losses			295
Retirement benefit assets at 31 December 2012			**33**

Of the expense for the year, €23m (2011: €23m) has been included in the income statement within staff costs (see Note 3). Actuarial gains and losses have been reported in other comprehensive income.

The Group expects to contribute €40m to its defined benefit pension schemes in 2013.

	Group and Bank		
Changes in value of net pension asset/(liability)	**Fair value of plan assets €m**	**Present value of defined benefit obligations €m**	**Net pension asset/(liability) €m**
At 1 January 2011	717	(753)	(36)
Income statement:			
Expected return	44	-	44
Interest cost	-	(42)	(42)
Current service cost	-	(24)	(24)
Past service cost	-	(1)	(1)
	44	(67)	(23)
Statement of comprehensive income:			
Actuarial (loss)/gain	(61)	35	(26)
Contributions by employer	42	-	42
Contributions by plan participants	4	(4)	-
Benefits paid	(23)	23	-
At 31 December 2011	723	(766)	(43)
Unrecognised actuarial losses			54
Retirement benefit assets at 31 December 2011			**11**

4. Pension costs (continued)

History of defined benefit schemes (Group and Bank)	2012 €m	2011 €m	2010 €m	2009 €m	2008 €m
Present value of defined benefit obligations	(1,093)	(766)	(753)	(667)	(671)
Fair value of plan assets	831	723	717	503	409
Net deficit	(262)	(43)	(36)	(164)	(262)
Experience gains on plan liabilities (1)	5	7	97	11	26
Experience gains/(losses) on plan assets	44	(61)	23	47	(196)
Actual return on pension scheme assets	83	(17)	63	74	(159)

(1) 2011 experience gains on plan liabilities have been adjusted to exclude the impact of changes in actuarial assumptions.

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

	Group and Bank			
	(Decrease)/increase in pension cost for the year		(Decrease)/increase in obligation at 31 December	
	2012 €m	2011 €m	2012 €m	2011 €m
0.25% increase in the discount rate	(4)	(2)	(59)	(32)
0.25% increase in inflation	5	4	64	34
0.25% additional rate of increase in pensions in payment	3	2	34	19
0.25% additional rate of increase in deferred pensions	0	-	8	4
0.25% additional rate of increase in salaries	2	2	20	11
Longevity increase of 1 year	2	1	22	13

The Finance (No.2) Act 2011 introduced a levy at the rate of 0.6% per annum for each of the four years, 2011 to 2014. The Act states that payment is due by 25 September each year. The levy is payable on all of a scheme's assets (other than "excluded assets") and is recognised in the income statement as a reduction in the expected return of assets. An amount of €4.4m (excluding Additional Voluntary Contributions) was deducted from the asset value of the Ulster Bank Pension Scheme (Republic of Ireland) and First Active Pension Schemes within the statutory deadlines (2011: €4.4m).

5. Emoluments of directors

	2012 €	2011 €
Emoluments for the provision of directors' services:		
Non-executive directors - emoluments	124,752	89,908
Chairman and executive directors - emoluments	1,128,854	1,651,371
Contributions and allowances in respect of pension schemes	36,978	50,055
Total emoluments received by directors	1,290,584	1,791,334

The emoluments include an allocation of the remuneration paid by other Group companies for all of the executive directors in respect of their services to the Bank. The emoluments have been incurred wholly for services as directors during the year.

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

During the year there were no emoluments in respect of compensation payments for loss of office (2011: €336,732).

The executive directors may also participate in the RBS Group's executive share option and sharesave schemes. Details of their interests in the RBS Group shares arising from their participation are given in Note 32.

On the 5 July 2012, the Group CEO Jim Brown informed the Board of Directors that he did not wish to be considered for an annual bonus award for 2012.

6. Taxation

	Group	
	2012	2011
Current taxation:	**€m**	€m
Corporation Tax		
Credit for the year	**9**	3
(Under)/over provision in respect of prior periods	**(4)**	30
Total current taxation	**5**	33
Deferred taxation:		
(Charge)/credit for the year	**(6)**	75
(Under)/over provision in respect of prior periods	**(246)**	6
Total deferred taxation	**(252)**	81
Tax (charge)/credit for the year	**(247)**	114

The standard rate of tax for the year, based on the Irish standard rate of Corporation Tax is 12.5% (2011: 12.5%). The actual tax charge for the current and previous year differs from the standard rate for the reasons set out below:

	2012	2011
	€m	€m
Operating loss before taxation	**(2,141)**	(2,811)
Tax credit on operating loss at the standard rate	**268**	351
Factors affecting the credit for the year:		
Unrecognised losses	**(259)**	(292)
De-recognition of a deferred tax asset	**(250)**	-
Other timing differences	**(6)**	16
Tax arising at rates other than the standard rate of tax	**-**	3
Adjustments to tax credit in respect of prior periods	**-**	36
Actual tax (charge)/credit for the year	**(247)**	114

The effective tax rate for the year was (11.5%) (2011: 4.1%).

7. Loss dealt with in the financial statements of the Bank

In accordance with section 148(8) of the Companies Act, 1963 and Section 7(1A) of the Companies (Amendment) Act 1986, the Bank is availing of the exemption from presenting its individual Income Statement and from filing it with the Registrar of Companies. The Bank's loss for the financial year, determined in accordance with IFRS as adopted by the EU, was €2,343m (2011: €2,829m).

NOTES TO THE FINANCIAL STATEMENTS *for the year ended 31 December 2012*

8. Financial instruments

The following tables analyse the financial assets and financial liabilities in accordance with the categories of financial instruments in accordance with IAS 39. Assets and liabilities outside the scope of IAS 39 are shown separately.

	Group						
2012	Held-for-trading €m	Designated as at fair value through profit or loss €m	Available-for-sale €m	Loans and receivables €m	Other (amortised cost) €m	Non financial assets/ liabilities €m	**Total €m**
Assets							
Cash and balances at central banks	-	-	-	221	-	-	**221**
Loans and advances to banks (1) (5)	16	-	-	4,066	-	-	**4,082**
Loans and advances to customers (2) (5)	-	30	-	35,146	-	-	**35,176**
Equity shares	-	-	8	-	-	-	**8**
Derivatives	983	-	-	-	-	-	**983**
Property, plant and equipment	-	-	-	-	-	270	**270**
Prepayments, accrued income and other assets	-	-	-	-	-	50	**50**
Retirement benefit assets	-	-	-	-	-	33	**33**
Deferred taxation	-	-	-	-	-	89	**89**
	999	30	8	39,433	-	442	**40,912**
Liabilities							
Deposits by banks (3) (6)	71	-	-	-	6,201	-	**6,272**
Customer accounts (6)	-	2,076	-	-	17,821	-	**19,897**
Debt securities in issue (4)	-	-	-	-	3,989	-	**3,989**
Derivatives	1,260	-	-	-	-	-	**1,260**
Accruals, deferred income and other liabilities	-	-	-	-	-	286	**286**
Deferred taxation	-	-	-	-	-	4	**4**
Subordinated liabilities	-	-	-	-	956	-	**956**
	1,331	2,076	-	-	28,967	290	**32,664**
Equity							**8,248**
							40,912

For notes relating to this table refer to page 33.

ULSTER BANK IRELAND LIMITED

NOTES TO THE FINANCIAL STATEMENTS *for the year ended 31 December 2012*

8. Financial instruments (continued)

	Group						
2011	Held-for-trading €m	Designated as at fair value through profit or loss €m	Available-for-sale €m	Loans and receivables €m	Other (amortised cost) €m	Non financial assets/ liabilities €m	Total €m
Assets							
Cash and balances at central banks	-	-	-	272	-	-	272
Loans and advances to banks (1) (5)	25	-	-	3,379	-	-	3,404
Loans and advances to customers (2) (5)	-	38	-	38,975	-	-	39,013
Debt securities	-	-	32	-	-	-	32
Equity shares	-	-	6	-	-	-	6
Derivatives	1,245	-	-	-	-	-	1,245
Property, plant and equipment	-	-	-	-	-	265	265
Prepayments, accrued income and other assets	-	-	-	-	-	47	47
Retirement benefit assets	-	-	-	-	-	11	11
Deferred taxation	-	-	-	-	-	341	341
	1,270	38	38	42,626	-	664	44,636
Liabilities							
Deposits by banks (3) (6)	71	-	-	-	12,235	-	12,306
Customer accounts (6)	8	1,583	-	-	16,375	-	17,966
Debt securities in issue (4)	-	-	-	-	4,175	-	4,175
Derivatives	1,673	-	-	-	-	-	1,673
Accruals, deferred income and other liabilities	-	-	-	-	-	324	324
Deferred taxation	-	-	-	-	-	1	1
Subordinated liabilities	-	-	-	-	946	-	946
	1,752	1,583	-	-	33,731	325	37,391
Equity							7,245
							44,636

Notes:

(1) Includes repurchase agreements of €nil (2011: €nil) and items in the course of collection from other banks of €155m (2011: €148m) for Group and Bank.

(2) Ulster Bank Ireland Limited has advances secured on residential property subject to non-recourse funding. Under IAS 39, these securitised mortgages qualify for full recognition on the balance sheet at 31 December 2012 and are included in loans and advances to customers. As at 31 December 2012 €12,987m (2011: €13,998m) are included in loans and advances to customers.

(3) Includes repurchase agreements of €2,300m (2011: €1,651m) and items in the course of transmission to other banks of €267m (2011: €142m) for Group and Bank.

(4) Comprises Bonds and medium term notes of €3,946m (2011: €4,152m) and Certificates of deposit and other commercial paper of €43m (2011: €23m).

(5) Includes amounts due from parent or fellow RBS Group undertakings

(6) Includes amounts due to parent or fellow RBS Group undertakings

8. Financial instruments (continued)

2012	Bank						
	Held-for-trading €m	Designated as at fair value through profit or loss €m	Available-for-sale €m	Loans and receivable €m	Other (amortised cost) €m	Non financial assets/ liabilities €m	Total €m
Assets							
Cash and balances at central banks	-	-	-	221	-	-	**221**
Loans and advances to banks (1)	16	-	-	2,997	-	-	**3,013**
Loans and advances to customers (1)	-	30	-	37,643	-	-	**37,673**
Debt securities	-	-	-	11,079	-	-	**11,079**
Equity shares	-	-	8	-	-	-	**8**
Investments in Group undertakings	-	-	-	-	-	191	**191**
Derivatives	980	-	-	-	-	-	**980**
Property, plant and equipment	-	-	-	-	-	160	**160**
Prepayments, accrued income and other assets	-	-	-	-	-	46	**46**
Retirement benefit assets	-	-	-	-	-	33	**33**
Deferred taxation	-	-	-	-	-	89	**89**
	996	30	8	51,940	-	519	**53,493**
Liabilities							
Deposits by banks (2)	51	-	-	-	6,154	-	**6,205**
Customer accounts (2)	-	2,076	-	-	34,836	-	**36,912**
Debt securities in issue	-	-	-	-	43	-	**43**
Derivatives	1,076	-	-	-	-	-	**1,076**
Accruals, deferred income and other liabilities	-	-	-	-	-	280	**280**
Deferred taxation	-	-	-	-	-	4	**4**
Subordinated liabilities	-	-	-	-	956	-	**956**
	1,127	2,076	-	-	41,989	284	**45,476**
Equity							**8,017**
							53,493

2011	Bank						
	Held-for-trading €m	Designated as at fair value through profit or loss €m	Available-for-sale €m	Loans and receivable €m	Other (amortised cost) €m	Non financial assets/ liabilities €m	Total €m
Assets							
Cash and balances at central banks	-	-	-	272	-	-	272
Loans and advances to banks (1)	25	-	-	2,249	-	-	2,274
Loans and advances to customers (1)	-	61	-	41,216	-	-	41,277
Debt securities	-	-	32	12,548	-	-	12,580
Equity shares	-	-	6	-	-	-	6
Investments in Group undertakings	-	-	-	-	-	191	191
Derivatives	1,125	-	-	-	-	-	1,125
Property, plant and equipment	-	-	-	-	-	184	184
Prepayments, accrued income and other assets	-	-	-	-	-	30	30
Retirement benefit assets	-	-	-	-	-	11	11
Deferred taxation	-	-	-	-	-	341	341
	1,150	61	38	56,285	-	757	58,291
Liabilities							
Deposits by banks (2)	71	-	-	-	12,248	-	12,319
Customer accounts (2)	8	1,583	-	-	34,799	-	36,390
Debt securities in issue	-	-	-	-	23	-	23
Derivatives	1,325	-	-	-	-	-	1,325
Accruals, deferred income and other liabilities	-	-	-	-	-	310	310
Deferred taxation	-	-	-	-	-	1	1
Subordinated liabilities	-	-	-	-	946	-	946
	1,404	1,583	-	-	48,016	311	51,314
Equity							6,977
							58,291

(1) Includes amounts due from parent or fellow group undertakings.
(2) Includes amounts due to parent or fellow group undertakings.

8. Financial instruments (continued)

The following table shows the financial instruments carried at fair value by valuation method.

	Group							
	2012				2011			
	Level 1(1) €m	**Level 2(2) €m**	**Level 3(3) €m**	**Total €m**	Level 1 €m	Level 2 €m	Level 3 €m	Total €m
Assets								
Loans and advances to banks	-	16	-	16	-	25	-	25
Loans and advances to customers	-	30	-	30	-	38	-	38
Debt securities	-	-	-	-	32	-	-	32
Equity shares	-	8	-	8	-	6	-	6
Derivatives	-	983	-	983	-	1,245	-	1,245
Total	-	1,037	-	1,037	32	1,314	-	1,346
Liabilities								
Deposits by banks	-	71	-	71	-	71	-	71
Deposits by customers	-	2,076	-	2,076	-	1,591	-	1,591
Derivatives	-	1,260	-	1,260	-	1,673	-	1,673
Total	-	3,407	-	3,407	-	3,335	-	3,335

	Bank							
	2012				2011			
	Level 1(1) €m	**Level 2(2) €m**	**Level 3(3) €m**	**Total €m**	Level 1 €m	Level 2 €m	Level 3 €m	Total €m
Assets								
Loans and advances to banks	-	16	-	16	-	25	-	25
Loans and advances to customers	-	30	-	30	-	61	-	61
Debt securities	-	-	-	-	32	-	-	32
Equity shares	-	8	-	8	-	6	-	6
Derivatives	-	980	-	980	-	1,125	-	1,125
Total	-	1,034	-	1,034	32	1,217	-	1,249
Liabilities								
Deposits by banks	-	51	-	51	-	71	-	71
Deposits by customers	-	2,076	-	2,076	-	1,591	-	1,591
Derivatives	-	1,076	-	1,076	-	1,325	-	1,325
Total	-	3,203	-	3,203	-	2,987	-	2,987

(1) Valued using unadjusted quoted prices in active markets for identical financial instruments. This category includes listed equity shares, certain exchange-traded derivatives, G10 government securities and certain US agency securities.

(2) Valued using techniques based significantly on observable market data. Instruments in this category are valued using:
a) quoted prices for similar instruments or identical instruments in markets which are not considered to be active: or
b) valuation techniques where all the inputs that have a significant effect on the valuation are directly or indirectly based on observable market data.

The type of instruments that trade in markets that are not considered to be active, but are based on quoted market prices, broker dealer quotations or alternative pricing sources with reasonable levels of price transparency and those instruments valued using techniques include most government agency securities, investment-grade corporate bonds, certain mortgage products, certain bank and bridge loans, repos and reverse repos, less liquid equities, state and municipal obligations, most physical commodities, investment contracts issued by the Group's life assurance businesses and certain money market securities and loan commitments and most OTC derivatives.

(3) Instruments in this category have been valued using a valuation technique where at least one input (which could have a significant effect on the instrument's valuation) is not based on observable market data. Where inputs can be observed from market data without undue cost and effort, the observed input is used. Otherwise, the Group determines a reasonable level for the input.

Financial instruments included within Level 3 of the fair value hierarchy primarily consist of cash instruments which trade infrequently, certain syndicated and commercial mortgage loans, unlisted equity shares, certain residual interests in securitisations, super senior tranches of high grade and mezzanine collaterised debt obligations (CDO's), and other mortgage-based 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.

ULSTER BANK IRELAND LIMITED

NOTES TO THE FINANCIAL STATEMENTS *for the year ended 31 December 2012*

8. Financial instruments (continued)

The following tables show the carrying values and the fair values of financial instruments on the balance sheet carried at amortised cost.

	Group			
	2012 Carrying value €m	**2012 Fair value €m**	2011 Carrying value €m	2011 Fair value €m
Financial assets				
Cash and balances at central banks	**221**	**221**	272	272
Loans and advances to banks	**4,066**	**4,066**	3,379	3,380
Loans and advances to customers	**35,146**	**27,814**	38,975	30,461
Financial liabilities				
Deposits by banks	**6,201**	**6,201**	12,235	12,236
Customer accounts	**17,821**	**17,928**	16,375	16,505
Debt securities in issue	**3,989**	**2,646**	4,175	2,501
Subordinated liabilities	**956**	**956**	946	947

	Bank			
	2012 Carrying value €m	**2012 Fair value €m**	2011 Carrying value €m	2011 Fair value €m
Financial assets				
Cash and balances at central banks	**221**	**221**	272	272
Loans and advances to banks	**2,997**	**2,997**	2,249	2,249
Loans and advances to customers	**37,643**	**30,311**	41,216	32,726
Debt securities	**11,079**	**7,309**	12,548	12,548
Financial liabilities				
Deposits by banks	**6,154**	**6,154**	12,248	12,249
Customer accounts	**34,836**	**34,943**	34,799	32,983
Debt securities in issue	**43**	**43**	23	23
Subordinated liabilities	**956**	**956**	946	947

8. Financial instruments (continued)

The fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. 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.

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. As a wide range of valuation techniques is available, it may be inappropriate to compare the Group's fair value information to independent markets or other financial institutions' fair values.

The assumptions and methodologies underlying the calculation of fair values of financial instruments at the balance sheet date are set out below:

The fair value of financial instruments that are of short maturity (3 months or less) approximates their carrying value. This applies mainly to 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 and demand deposits.

The Group uses a number of methodologies to determine the fair values of financial instruments for which observable prices in active markets for identical instruments are not available. These techniques include: relative value methodologies based on observable prices for similar instruments; present value approaches where future cash flows from the asset or liability are estimated and then discounted using a risk-adjusted interest rate; option pricing models (such as Black-Scholes or binomial option pricing models) and simulation models such as Monte-Carlo.

The principal inputs to these valuation techniques are listed below. 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.

- 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 European Interbank Offered Rate (EURIBOR) and quoted interest rates in the swap, bond and futures markets.
- Foreign currency exchange rates - there are observable markets both for spot and forward contracts and futures in the world's major currencies.

Loans and advances to banks and customers
Fair value is estimated by grouping loans into homogeneous portfolios and applying a discount rate to the cash flows. The discount rate is based on the market rate applicable at the balance sheet date for a similar portfolio with similar maturity and credit risk characteristics.

Deposits by banks and customer accounts
The fair values of deposits are estimated using discounted cash flow valuation techniques.

8. Financial instruments (continued)

Remaining maturity

	Group		
2012	Less than 12 months €m	More than 12 months €m	**Total €m**
Assets			
Cash and balances at central banks	221	-	**221**
Loans and advances to banks	4,078	4	**4,082**
Loans and advances to customers	7,924	27,252	**35,176**
Equity shares	-	8	**8**
Derivatives	119	864	**983**
Liabilities			
Deposits by banks	4,862	1,410	**6,272**
Customer accounts	17,790	2,107	**19,897**
Debt securities in issue	39	3,950	**3,989**
Derivatives	106	1,154	**1,260**
Subordinated liabilities	77	879	**956**

	Group		
2011	Less than 12 months €m	More than 12 months €m	Total €m
Assets			
Cash and balances at central banks	272	-	272
Loans and advances to banks	3,404	-	3,404
Loans and advances to customers	7,634	31,379	39,013
Debt securities	10	22	32
Equity shares	-	6	6
Derivatives	237	1,008	1,245
Liabilities			
Deposits by banks	12,077	229	12,306
Customer accounts	16,231	1,735	17,966
Debt securities in issue	6	4,169	4,175
Derivatives	161	1,512	1,673
Subordinated liabilities	-	946	946

8. Financial instruments (continued)

Remaining maturity (continued)

	Bank		
2012	Less than 12 months €m	More than 12 months €m	**Total €m**
Assets			
Cash and balances at central banks	221	-	**221**
Loans and advances to banks	3,009	4	**3,013**
Loans and advances to customers	10,424	27,249	**37,673**
Debt securities	11,079	-	**11,079**
Equity shares	-	8	**8**
Derivatives	119	861	**980**
Liabilities			
Deposits by banks	4,795	1,410	**6,205**
Customer accounts	34,650	2,262	**36,912**
Debt securities in issue	39	4	**43**
Derivatives	104	972	**1,076**
Subordinated liabilities	77	879	**956**

	Bank		
2011	Less than 12 months €m	More than 12 months €m	Total €m
Assets			
Cash and balances at central banks	272	-	272
Loans and advances to banks	2,274	-	2,274
Loans and advances to customers	9,655	31,622	41,277
Debt securities	12,559	21	12,580
Equity shares	-	6	6
Derivatives	357	768	1,125
Liabilities			
Deposits by banks	12,088	231	12,319
Customer accounts	19,714	16,676	36,390
Debt securities in issue	6	17	23
Derivatives	136	1,189	1,325
Subordinated liabilities	-	946	946

9. Financial assets - impairment

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

	Group and Bank			
	Individually assessed €m	**Collectively assessed €m**	**Latent €m**	**Total €m**
At 1 January 2012	**6,657**	**1,366**	**611**	**8,634**
Currency translation and other adjustments	**17**	**1**	**1**	**19**
Transfer	**(215)**	**215**	**-**	**-**
Amounts written-off [1]	**(80)**	**(46)**	**-**	**(126)**
Charged to the income statement	**1,247**	**905**	**285**	**2,437**
Unwind of discount	**(213)**	**(36)**	**-**	**(249)**
At 31 December 2012[2]	**7,413**	**2,405**	**897**	**10,715**

	Group and Bank			
	Individually assessed €m	Collectively assessed €m	Latent €m	Total €m
At 1 January 2011	4,326	723	560	5,609
Currency translation and other adjustments	22	-	1	23
Amounts written-off [1]	(148)	(30)	-	(178)
Charged to the income statement	2,661	702	50	3,413
Unwind of discount	(204)	(29)	-	(233)
At 31 December 2011[2]	6,657	1,366	611	8,634

(1) Amounts written off do not include any loans and advances to banks.
(2) Impairment losses at 31 December 2012 and 31 December 2011 do not include any loans and advances to banks.

Loan impairment

At 31 December 2012, the non-accrual loans and loans past due 90 days amounted to €19,235m (2011: €16,598m) for both Group and Bank. Loan impairment provisions of €9,818m (2011: €8,023m) were held against the loans:

	Group and Bank	
	2012 €m	2011 €m
Gross income not recognised but which would have been recognised under the original terms of non-accrual and restructured loans		
Domestic	**1,482**	973

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

The following table shows analysis of impaired financial assets:

	2012			2011		
Group and Bank	**Cost €m**	**Provision €m**	**Carrying amount €m**	Cost €m	Provision €m	Carrying amount €m
Impaired financial assets						
Loans and advances to customers	**18,521**	**(9,818)**	**8,703**	16,288	(8,023)	8,265
Equity shares	**10**	**(2)**	**8**	8	(2)	6
	18,531	**(9,820)**	**8,711**	16,296	(8,025)	8,271

The Group holds collateral in respect of certain loans and advances to banks and to customers that are past due or impaired. Such collateral includes mortgages over property (both personal and commercial); charges over business assets such as plant, inventories and trade receivables; and guarantees of lending from parties other than the borrower.

9. Financial assets - impairment (continued)

The following table shows financial and non-financial assets, recognised on the Group and Bank's balance sheets, obtained during the year by taking possession of collateral or calling on other credit enhancements:

	Group	
	2012	2011
	€m	€m
Residential property	**31**	21
Other property	**24**	5
	55	26

	Bank	
	2012	2011
	€m	€m
Residential property	**24**	21
Other property	**2**	-
	26	21

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

Group and Bank	**Past due 1-29 days**	**Past due 30-59 days**	**Past due 60-89 days**	**Past due more than 90 days**	**Total**
2012	**€m**	**€m**	**€m**	**€m**	**€m**
Loans and advances to customers	**1,435**	**625**	**437**	**714**	**3,211**
2011					
Loans and advances to customers	1,527	653	482	310	2,972

	Group and Bank	
	2012	2011
	€m	€m
Impaired financial assets - individually assessed:		
Loans and advances to customers	**7,413**	6,657

Loans that have been renegotiated in the past 12 months that would otherwise have been past due or impaired amounted to €3,144m as at 31 December 2012 (2011: €3,400m) for the Group and Bank.

10. Debt securities

	Group					
	2012			2011		
	Other central and local government	**Mortgage backed securities**	**Total**	Other central and local government	Mortgage backed securities	Total
	€m	**€m**	**€m**	€m	€m	€m
Available-for-sale	**-**	**-**	**-**	32	-	32
Gross unrealised gains	**-**	**-**	**-**	1	-	1

10. Debt securities (continued)

	Bank					
	2012			2011		
	Other central and local government €m	**Mortgage backed securities €m**	**Total €m**	Other central and local government €m	Mortgage backed securities €m	Total €m
Available-for-sale	-	-	-	32	-	32
Loans and receivables	-	11,079	11,079	-	12,548	12,548
	-	11,079	11,079	32	12,548	12,580
Available-for-sale Gross unrealised gains	-	-	-	1	-	1

Mortgage backed securities included within the Bank consist solely of balances with other Group companies.

11. Equity shares

	Group and Bank	
	2012 Unlisted €m	2011 Unlisted €m
Available-for-sale	8	6

No gains or losses were realised on the available-for-sale equity shares (2011: €nil).

Unquoted equity investments whose fair value cannot be reliably measured are carried at cost and classified as available-for-sale financial assets.

12. Investments in Group undertakings

Investments in Group undertakings are carried at cost less impairment.

	Bank	
	2012 €m	2011 €m
At 1 January and 31 December	191	191

The principal subsidiary undertakings of the Bank are shown below. Their capital consists of ordinary shares which are unlisted. All of these undertakings are owned directly or indirectly through intermediate holding companies and are all wholly-owned.

Undertaking	Nature of business	Place of incorporation
Ulster Bank Investment Funds Limited	Fund administration services	Republic of Ireland
Easycash (Ireland) Limited	Provision of ATMs in convenient locations	Republic of Ireland
Ulster Bank Wealth	Wealth management services	Republic of Ireland

Full list of subsidiary undertakings

In presenting details of its subsidiary undertakings, the exemption permitted by Regulation 10 of the European Communities (Credit Institutions: Accounts) Regulations, 1992, has been availed of. A full list of subsidiary undertakings will be annexed to the annual return for the Bank. All of these undertakings are included in the Group's consolidated financial statements and have an accounting reference date of 31 December.

There are a number of entities in which the Group holds less than half the voting rights which are consolidated when the substance of the relationship between the Group and the entity indicates that the entity is controlled by the Group. Such entities are deemed to be controlled by the Group when relationships with such entities give rise to benefits that are in substance no different from those that would arise were the entity a subsidiary.

13. Intangible assets

Intangible assets comprising goodwill, computer software and other acquired intangibles were fully impaired as at 31 December 2012 and 31 December 2011. No further intangible assets were developed or acquired in the current or the previous year.

14. Property, plant and equipment

	Group					
2012	Investment properties €m	Freehold land and buildings €m	Leases of 50 years or more unexpired €m	Leases of 50 years or less unexpired €m	Computer and other equipment €m	**Total €m**
Cost:						
At 1 January 2012	77	120	24	87	149	**457**
Additions	31	-	-	3	5	**39**
Disposals	-	-	-	(2)	-	**(2)**
At 31 December 2012	108	120	24	88	154	**494**
Accumulated depreciation and amortisation:						
At 1 January 2012	-	49	15	24	104	**192**
Disposals	-	-	-	(1)	-	**(1)**
Impairments	-	10	1	-	-	**11**
Depreciation charge for the year	-	3	1	8	10	**22**
At 31 December 2012	-	62	17	31	114	**224**
Carrying amount at 31 December 2012	**108**	**58**	**7**	**57**	**40**	**270**

There was no profit or loss on disposals of freehold land and buildings in 2011.

Rental income from investment properties was €5m (2011: €2m). During the year there were €3m direct operating expenses of investment properties (2011: €2m) and €13m direct operating expenses of investment properties not generating rental income (2011: €10m).

14. Property, plant and equipment (continued)

	Group					
2011	Investment properties €m	Freehold land and buildings €m	Leases of 50 years or more unexpired €m	Leases of 50 years or less unexpired €m	Computer and other equipment €m	Total €m
Cost:						
At 1 January 2011	131	121	18	111	148	529
Reclassifications	12	-	14	(26)	-	-
Additions	5	-	-	2	2	9
Disposals	-	(1)	(8)	-	(1)	(10)
Revaluation	(71)	-	-	-	-	(71)
At 31 December 2011	77	120	24	87	149	457
Accumulated depreciation and amortisation:						
At 1 January 2011	3	46	10	16	95	170
Reclassifications	(3)	-	3	-	-	-
Disposals	-	-	-	-	(1)	(1)
Depreciation charge for the year	-	3	2	8	10	23
At 31 December 2011	-	49	15	24	104	192
Carrying amount at 31 December 2011	77	71	9	63	45	265

	Bank					
2012	Investment properties €m	Freehold land and buildings €m	Leases of 50 years or more unexpired €m	Leases of 50 years or less unexpired €m	Computer and other equipment €m	**Total €m**
Cost:						
At 1 January 2012	-	118	18	87	138	**361**
Additions	2	-	-	3	2	**7**
Disposals	-	-	-	(2)	-	**(2)**
At 31 December 2012	2	118	18	88	140	**366**
Accumulated depreciation and amortisation:						
At 1 January 2012	-	49	10	24	94	**177**
Disposals	-	-	-	(1)	-	**(1)**
Impairments	-	10	1	-	-	**11**
Depreciation charge for the year	-	2	1	7	9	**19**
At 31 December 2012	-	61	12	30	103	**206**
Carrying amount at 31 December 2012	**2**	**57**	**6**	**58**	**37**	**160**

14. Property, plant and equipment (continued)

	Bank				
	Freehold land and buildings	Leases of 50 years or more unexpired	Leases of 50 years or less unexpired	Computer and other equipment	Total
2011	€m	€m	€m	€m	€m
Cost:					
At 1 January 2011	119	18	85	137	359
Additions	-	-	2	2	4
Disposals	(1)	-	-	(1)	(2)
At 31 December 2011	118	18	87	138	361
Accumulated depreciation and amortisation:					
At 1 January 2011	46	10	16	86	158
Disposals	-	-	-	(1)	(1)
Depreciation charge for the year	3	-	8	9	20
At 31 December 2011	49	10	24	94	177
Carrying amount at 31 December 2011	69	8	63	44	184

15. Derivatives

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

	Group					
	2012			2011		
	Notional amounts €m	**Assets €m**	**Liabilities €m**	Notional amounts €m	Assets €m	Liabilities €m
Free standing derivatives						
Exchange rate contracts:						
Spot, forwards and futures	**2,102**	**13**	**19**	4,679	148	83
Currency swaps	**1,834**	**68**	**216**	1,838	62	234
Interest rate contracts:						
Interest rate swaps	**61,153**	**772**	**1,022**	62,712	970	1,342
Options purchased	**206**	**-**	**-**	391	6	-
Options written	**233**	**-**	**-**	259	-	6
Futures and forwards	**619**	**3**	**3**	1,506	8	8
Equity and commodity contracts	**2,369**	**127**	**-**	1,431	51	-
	68,516	**983**	**1,260**	72,816	1,245	1,673

15. Derivatives (continued)

	Bank					
	2012			2011		
	Notional amounts €m	**Assets €m**	**Liabilities €m**	Notional amounts €m	Assets €m	Liabilities €m
Free standing derivatives						
Exchange rate contracts:						
Spot, forwards and futures	**2,102**	**13**	**19**	4,679	148	83
Currency swaps	**1,117**	**68**	**66**	1,090	61	60
Interest rate contracts:						
Interest rate swaps	**49,768**	**769**	**988**	47,614	851	1,168
Options purchased	**206**	**-**	**-**	261	6	-
Options written	**233**	**-**	**-**	259	-	6
Futures and forwards	**619**	**3**	**3**	1,506	8	8
Equity and commodity contracts	**2,369**	**127**	**-**	1,431	51	-
	56,414	**980**	**1,076**	56,840	1,125	1,325

16. Prepayments, accrued income and other assets

	Group		Bank	
	2012 €m	2011 €m	**2012 €m**	2011 €m
Prepayments	**14**	21	**11**	14
Accrued income	**9**	11	**5**	7
Other assets	**27**	15	**30**	9
	50	47	**46**	30

17. Accruals, deferred income and other liabilities

	Group		Bank	
	2012 €m	2011 €m	**2012 €m**	2011 €m
Accruals	**180**	209	**177**	206
Deferred income	**2**	7	**2**	7
Other liabilities	**104**	108	**101**	97
	286	324	**280**	310

Provisions of €90m (2011: €65m) for the Group and €88m (2011: €63m) for the Bank are included in other liabilities.

The following amounts are included within provisions:

	Group			
	Property provisions €m	**Other provisions €m**	**PPI provisions €m**	**Total Provisions €m**
Provisions as at 1 January 2012	61	4	-	**65**
Charge to the income statement	11	40	7	**58**
Utilised in year	(14)	(20)	-	**(34)**
Other Movements	-	-	4	**4**
Released during the year	(3)	-	-	**(3)**
Provisions as at 31 December 2012	**55**	**24**	**11**	**90**

17. Accruals, deferred income and other liabilities (continued)

	Bank			
	Property provisions €m	**Other provisions €m**	**PPI provisions €m**	**Total Provisions €m**
Provisions as at 1 January 2012	61	2	-	**63**
Charge to the income statement	11	40	7	**58**
Utilised in year	(14)	(20)	-	**(34)**
Other Movements	-	-	4	**4**
Released during the year	(3)	-	-	**(3)**
Provisions as at 31 December 2012	**55**	**22**	**11**	**88**

Payment Protection Insurance (PPI)
The PPI provision was established to reflect current experience of PPI complaints received. The eventual cost is dependent upon complaint volumes, uphold rates and average redress costs. Assumptions relating to these are inherently uncertain and the ultimate financial impact may be different from the amount provided. The Group will continue to monitor the position closely and refresh its assumptions as more information becomes available.

18. Deferred taxation

Provision for deferred taxation has been made as follows:

	Group and Bank	
	2012 €m	2011 €m
Deferred tax asset	**89**	341
Deferred tax liability	**(4)**	(1)
Net deferred tax	**85**	340

	Group and Bank					
	Pension €m	Accelerated capital allowances €m	Deferred gains €m	Available for sale €m	Tax losses €m	Total €m
At 1 January 2011	1	-	(4)	(1)	262	258
(Charge)/credit to income statement	(2)	2	4	-	77	81
Other	-	-	-	1	-	1
At 1 January 2012	(1)	2	-	-	339	340
Charge to income statement	-	(2)	-	-	(250)	(252)
Charge to equity directly	(3)	-	-	-	-	(3)
At 31 December 2012	**(4)**	**-**	**-**	**-**	**89**	**85**

Deferred tax assets are recognised depending on the availability of future taxable profits in excess of profits arising from the reversal of other temporary differences. Economic and market pressures have continued to have a negative impact on future profit projections. Business projections prepared for impairment reviews indicate it is probable that sufficient future taxable income will be available against which to offset deferred tax assets of €89m within seven years. Therefore it has been appropriate to de-recognise the deferred tax asset carried at 1 January 2012 by €250m. Deferred tax assets of €1,087m (2011: €591m) have not been recognised in respect of tax losses carried forward.

19. Subordinated liabilities

	Group and Bank	
	2012 €m	2011 €m
Dated loan capital	**763**	755
Dated subordinated bonds	**77**	76
Perpetual subordinated bonds	**106**	105
Undated loan capital	**10**	10
	956	946

19. Subordinated liabilities (continued)

	Group and Bank	
	2012	2011
	€m	€m
Dated loan capital:		
Euro loan capital repayable 2022:		
- held by Ulster Bank Limited	**431**	431
Euro loan capital repayable 2022:		
- held by RBS plc	**100**	100
Euro (floating rate) repayable 2015:		
-held by First Active plc	**157**	149
Euro (floating rate) repayable 2020:		
- held by Ulster Bank Limited	**35**	35
Euro (floating rate) repayable 2019:		
- held by Ulster Bank Limited	**40**	40
	763	755
Dated subordinated bonds		
£60m 6.375% subordinated bonds 2018 (callable April 2013)		
- held by ABN AMRO	**77**	76
Perpetual subordinated bonds:		
Euro (fixed: 11.375%)	**63**	63
Sterling (fixed: 11.75%)	**41**	40
Sterling (floating rates)	**2**	2
	106	105
Undated loan capital		
Sterling loan capital - held by parent company	**10**	10
Total	**956**	946

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

Interest on Euro-denominated loan capital is payable quarterly at a margin over Euro Interbank Offer rates. Early repayment of the dated loan may take place at any time with a notice period of at least 30 days, subject to the prior agreement of the Central Bank of Ireland (CBI).

Dated subordinated bonds
The Sterling fixed subordinated bonds mature on 4 April 2018 but are callable on 4 April 2013. The claims of the holders of the bonds are subordinate to the claims of all trade payables of the Bank other than the holders of the perpetual subordinated bonds.

Perpetual subordinated bonds
The subordinated perpetual bonds were issued by First Active plc, in the Republic of Ireland, at par on conversion of First National Building Society to a public limited company pursuant to Section 107 of the Building Societies Act, 1989 to replace the issued fixed and floating rate permanent interest bearing shares of the Society. The claims of the holders of the bonds are subordinate to the claims of all creditors of the Bank.

Undated loan capital
The Sterling loan stock, which is perpetual, is held by another RBS Group company and is repayable at the option of the Bank only with prior consent of the CBI.

20. Share capital

	Group and Bank			
	Allotted, called up and fully paid		Authorised	
	1 January 2012 €m	31 December 2012 €m	2012 €m	2011 €m
Equity shares:				
Ordinary B shares of €1.27	1,825	1,825	2,223	2,223
Ordinary B shares of €1	1,745	1,745	2,400	2,400
Ordinary A shares of stg £1	22	22	37	37
Total share capital	3,592	3,592	4,660	4,660

	Allotted, called up and fully paid		Authorised	
Number of shares	**2012 Millions**	2011 Millions	**2012 Millions**	2011 Millions
Equity shares:				
Ordinary B shares of €1.27	1,437	1,437	1,750	1,750
Ordinary B shares of €1	1,745	1,745	2,400	2,400
Ordinary A shares of stg £1	15	15	25	25
Total share capital	3,197	3,197	4,175	4,175

All share classes rank pari passu in all respects.

21. Leases

Minimum amounts payable under non-cancellable leases:

	Group and Bank							
	2012				2011			
Year in which payment will occur:	**Within 1 year €m**	**After 1 year but within 5 years €m**	**After 5 years €m**	**Total €m**	Within 1 year €m	After 1 year but within 5 years €m	After 5 years €m	Total €m
Operating lease obligations: Future minimum lease payables:								
Premises	22	80	73	175	23	90	111	224
Equipment	1	2	-	3	2	2	-	4
	23	82	73	178	25	92	111	228

	Group and Bank	
	2012 €m	2011 €m
Amounts recognised as expense		
Operating lease payables - minimum payments	23	24

22. Collateral and securitisations

Securities repurchase agreements and lending transactions

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

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

The fair value (and carrying value) of securities transferred under repurchase transactions included within debt securities are shown on the balance sheet. Securities received as collateral under reverse repurchase agreements amounted to €18m (2011: €nil).

Other collateral given

	Group	
	2012	2011
Group assets charged as security for liabilities	**€m**	€m
Loans and advances to customers	**16,056**	17,828
Investment properties	**1**	23
Derivatives	**10**	10
	16,067	17,861

	Group	
	2012	2011
Liabilities secured by charges on assets	**€m**	€m
Debt securities in issue	**3,946**	4,151
Deposits by banks	**2,311**	1,650
Other liabilities	**-**	24
Derivatives	**32**	23
	6,289	5,848

Included in deposits by banks is the Group's obligation to the CBI under the terms of the Mortgage Backed Promissory Note programme. These obligations are secured by way of a floating charge to the CBI over all its right, title, interest and benefit.

Securitisations and other asset transfers

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

The following section aims to address the significant exposures which arise from the Group's activities through specific types of SPEs.

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

	2012		2011	
	Assets	**Liabilities**	Assets	Liabilities
	€m	**€m**	€m	€m
Residential mortgages	**12,987**	**3,946**	13,998	4,151
Corporate and commercial loans	**905**	**-**	1,137	-
	13,892	**3,946**	15,135	4,151

23. Risk management

The major risks associated with the Group's businesses are market, liquidity, credit, regulatory, reputational, conduct, operational and sovereign risk. The Group has established a comprehensive framework for managing these risks which is continually evolving as the Group's business activities change in response to market, credit, product and other developments. The Group is also exposed to risks from its defined benefit pension schemes.

The Group has established clear risk policies, including limits, reporting lines and control procedures. This framework is designed to provide tight control and is reviewed regularly by both Executive and Board Committees.

Market risk

Market risk is defined as the risk of loss as a result of adverse changes in market factors. The risk factors include interest rates, foreign currency and equity prices together with related parameters such as market volatilities.

The principal market risks to which the Group is exposed are interest rate and foreign exchange risks. The RBS Group manages market risk within its trading and non-trading portfolios through a comprehensive market risk management framework. This framework includes limits based on, but not limited to Value at Risk ("VaR"), scenario analysis, position and sensitivity analysis. The Group, in conjunction with the RBS Group Market Risk and Group Treasury, annually agree sub limits based on the Group's approved market risk appetite.

At the RBS Group level, the risk appetite is expressed in the form of a combination of VaR, sensitivity and scenario limits. VaR is a technique that produces estimates of the potential change in the market value of a portfolio over a specified time horizon at given confidence levels. For internal risk management purposes, the Group's VaR assumes a time horizon of one trading day and confidence level of 99% as it is considered that this provides greater clarity in respect of more severe potential economic outcomes. The Group's VaR model is based on a historical simulation model utilising data from the previous two years' trading results.

The VaR disclosure is broken down into trading and non-trading, where trading VaR relates to the trading activities and non-trading reflects the VaR associated with reclassified assets, money market business and the management of internal funds flow within the Group's businesses.

The Group calculates VaR using historical simulation models but does not make any assumption about the nature or type of underlying loss distribution other than implied by history. The methodology uses the previous 500 trading days of market data and calculates both general market risk (the risk due to movement in general market benchmarks) and idiosyncratic market risk (the risk due to movements in the value of securities by reference to specific issuers). The Group VaR should be interpreted in light of the limitations of the methodology used as follows:

- Historical simulation VaR may not provide the best estimate of future market movements. It can only provide a prediction of the future based on events that occurred in the time series horizon. Therefore, events that are more severe than those in the historical data series cannot be predicted;
- VaR that uses a 99% confidence level does not reflect the extent of potential losses beyond that percentile;
- VaR that uses a one-day time horizon will not fully capture the profit or loss implications of positions that cannot be liquidated or hedged within one day; and
- The Group computes the VaR of trading portfolios and non trading money markets portfolio at the close of business. Treasury Interest Rate risk VaR is computed monthly.

A 'Risks not in VaR' framework has been developed to address those market risks not adequately captured by the market standard VaR methodology. Where risks are not included in the model, various non-VaR controls (for example, position monitoring, sensitivity limits, triggers or stress limits) are in place. These limitations mean that the Group cannot guarantee that losses will not exceed the VaR.

(i) Trading portfolios

The Group eliminates its market risk in these portfolios by entering into back-to-back positions with its ultimate parent company, The Royal Bank of Scotland Group plc.

(ii) Non-trading

The principal market risks arising from the Group's non-trading activities are interest rate risk and currency risk. Non-trading risk is managed by both the Short Term Markets and Financing and Treasury, and arises from mismatches between the repricing of assets and liabilities in its wholesale markets, retail business and corporate bank.

23. Risk management - market risk (continued)

Total VaR

The short term financing and markets (STMF) desk is responsible for raising funding in the international wholesale and repo markets and funding the corporate loan book.

Total VaR is presented in the table below:

	31 December 2012 €m	**Maximum €m**	**Minimum €m**	**Average €m**
Value-at-Risk	**0.5**	**1.7**	**0.4**	**0.8**

	31 December 2011 €m	Maximum €m	Minimum €m	Average €m
Value-at-Risk	1.0	1.3	0.5	0.8

Interest rate VaR

The Interest Rate VaR limit is a sub limit of the Total VaR limit and is monitored daily.

Interest Rate VaR is presented in the table below:

	31 December 2012 €m	**Maximum €m**	**Minimum €m**	**Average €m**
Value-at-Risk	**0.5**	**1.7**	**0.4**	**0.8**

	31 December 2011 €m	Maximum €m	Minimum €m	Average €m
Value-at-Risk	1.0	1.2	0.4	0.7

Treasury Interest rate risk

The Group's portfolio of non-trading financial instruments principally comprises retail and commercial banking loans and deposits, debt securities issued, capital and hedging instruments.

Non-trading interest rate risk is calculated on the basis of establishing the repricing behaviour of each asset, liability and off-balance sheet product. For many products, the actual interest rate repricing characteristics differ from the contractual repricing. In most cases, the repricing maturity is determined by the market interest rate that most closely fits the historical behaviour of the product interest rate. For example with non-interest bearing current accounts, the repricing maturity is determined by the stability of the portfolio. The repricing maturities used are approved by RBS Group Treasury and the Ulster Bank Asset and Liability Committee (ALCO) at least annually. Key conventions are reviewed annually by ALCO. Short-term exposures are reviewed in terms of net interest income sensitivity over 12 months to a 1% parallel movement in interest rates. Risk is managed through arm's length cash transactions, bonds and derivatives, principally interest rate swaps.

A static maturity gap report is produced as at the month-end, in each functional currency based on the behavouralised repricing for each product. It is Group policy to include in the gap report non-financial assets and liabilities, mainly property, plant and equipment and the Group's capital and reserves, spread over medium and longer term maturities. This report also includes hedge transactions, principally derivatives.

Any residual non-trading interest rate exposures are controlled by limiting repricing mismatches in the balance sheets. Potential exposures to interest rate movements in the medium to long term are measured and controlled using a version of the same VaR methodology that is used for the Group's trading portfolios but without discount factors. Net accrual income exposures are measured and controlled in terms of sensitivity over time to movements in interest rates.

Risk is managed within VaR limits approved by ALCO through the execution of cash and derivative instruments. Execution of the hedging is carried out by the relevant division through the Group's Treasury function. The residual risk position is reported to ALCO and RBS Group Treasury on a monthly basis.

Non-trading interest rate VaR are Euro currency balances to which risk limits are applied. At 31 December 2012, Euro VaR was calculated to be €249,000 (2011: €464,000).

Principal amounts only are included. Average balances are used for products where this is considered to provide a more accurate representation of the exposure. A separate ladder is produced for each material currency.

23. Risk management - market risk (continued)

Treasury Interest rate risk (continued)

Option risk in the non-trading businesses principally occurs in certain fixed rate assets and liabilities. It arises where businesses undertake to provide funding to, or to accept deposits from, customers at a future date at a pre-determined fixed interest rate. Derivatives are used to manage the risk of interest rate movements from the date a commitment is made to a customer to the date the transaction closes. Option risk also arises where customers can repay fixed rate loans or withdraw fixed rate deposits prior to their maturity. In managing this risk, historic early repayment rates are taken into account.

The Group generally seeks to protect itself from early repayment risk through the imposition of contract breakage fees.

Foreign Exchange Risk in the Banking Book represents exposures to changes in the values of current holdings and future cash flows denominated in other currencies. Hedging instruments used to mitigate these risks include foreign currency options, currency swaps, futures, forwards and deposits. Foreign exchange risk results from the Group's investments in overseas subsidiaries, associates and branches in three principal forms:

- Structural foreign currency exposures that arise from net investment in overseas subsidiaries, associates and branches;
- Transactional/commercial foreign currency exposures that arise from mismatches in the currency balance sheet; and
- Treasury Interest Rate Risk VaR is computed monthly.

The Group does not maintain material non-trading 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 Group's policy in relation to structural positions is to match fund the structural foreign currency exposure arising from net asset value, including goodwill, in foreign subsidiaries, equity accounted investments and branches, except where doing so would materially increase the sensitivity of either the Group's or the subsidiary's regulatory capital ratios to currency movements. The policy requires structural foreign exchange positions to be reviewed regularly by ALCO.

Foreign exchange differences arising on the translation of foreign operations are recognised directly in equity together with the effective portion of foreign exchange differences arising on hedging liabilities.

The table below sets out the Group's structural foreign currency exposures as at 31 December 2012:

2012	**Net assets of overseas investment €m**	**Minority interest €m**	**Net investments €m**	**Currency borrowings €m**	**Economic hedges €m**	**Structural foreign currency exposures €m**
GBP	296	-	296	-	-	296

2011	Net assets of overseas investment €m	Minority interest €m	Net investments €m	Currency borrowings €m	Economic hedges €m	Structural foreign currency exposures €m
GBP	288	-	288	-	-	288

At 31 December 2012, a 5% strengthening of foreign currencies would result in a structural foreign currency gain of €15m in equity (2011: €14m gain) and a 5% weakening of foreign currencies would result in a structural foreign currency loss of €15m in equity (2011: €14m loss).

Changes in foreign exchange rates affect the Group's earnings and equity through differences on the retranslation of the net assets and related funding of overseas subsidiaries from the local functional currency to Sterling. Gains or losses on foreign currency investments in subsidiary and associated undertakings, net of any losses or gains on related foreign currency funding, are recognised in reserves. In 2012 exchange gains of €8m (2011: losses €1m) have been charged to reserves.

23. Risk management (continued)

Liquidity risk

Safety and soundness of the balance sheet is one of the central pillars of the Group's restructuring strategy. The Group's ability to serve customers well and create value for shareholders is being built upon the foundations of a solid and strong balance sheet. Effective management of liquidity risk is central to the safety and soundness agenda.

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. Liquidity risk is highly dependent on company specific characteristics such as the maturity profile and composition of the Group's asset and liabilities, the quality and marketable value of its liquidity buffer and broader market factors, such as wholesale market conditions alongside depositor and investor behaviour.

The Group has in place a comprehensive set of policies to manage liquidity risk that reflected best market practice and complies with prevailing regulatory strictures. These policies have been comprehensively updated since 2008, reflecting:
- the Group's restructuring plan,
- regulatory developments and enhancements,
- ongoing instability in global financial markets, and
- more conservative expectations from the Group's various stakeholders.

These policies are designed to address three broad issues which ensure that:
- the Group maintains adequate liquidity resources to meet liabilities as and when they fall due;
- the Group maintains an adequate liquidity buffer appropriate to the business activities of the Group and their risk profile; and
- the Group has in place robust strategies, policies, systems and procedures for identifying, measuring, monitoring and managing liquidity risk.

At its simplest these policies determine the sources of liquidity risk and the steps the Group can take when these risks exceed certain tolerances. These include not only when and how to use the Group's liquidity buffer but also what other adjustments to the Group's balance sheet could be undertaken to manage these risks back within Group appetite. These policies are reviewed at least annually or sooner if the Group's own liquidity position changes or if market conditions and/or regulatory rules warrant further amendment or refinement.

Policy, framework and governance
The Group has in place a robust and comprehensive set of policies and procedures for assessing, measuring and managing the liquidity risk within the Group. This ensures that the Group always maintain sufficient eligible and appropriate financial resources to meet its forward looking financial commitments as they fall due.

Guided by ALCO, the Banks Board of directors are responsible for defining and approving the Group's liquidity policy and setting acceptable parameters and risk limits that align with the overall RBS Group standard and risk appetite. The Group's liquidity buffer is managed by the Treasury function who monitor and control the Group's funding and liquidity position.

Similar provisions and requirements exist for each entity within the Group whereby they must comply with both internal standards and local regulatory frameworks.

Liquidity Measurement and Monitoring
Liquidity risk is measured and assessed on a daily basis at the Group level in compliance with requirements laid out by the Central Bank of Ireland ("CBI"). The Group use a set of internal metrics and analysis to assess liquidity risk.

The Group uses limits to manage and control the overall extent of liquidity risk within the balance sheet. Limits will focus on the aggregate amount and composition of particular sources of liabilities, asset liability mismatches and third party counterparty concentrations.

As further described herein, stress testing is used to help inform a broader understanding of liquidity risk as well as to model specific liquidity risk events; for example the secession of a country from the Euro.

The Group actively monitors a range of market and firm specific indicators on an ongoing basis which are designed to act as early warning indicators that liquidity stresses are emerging. Some of these indicators will be based upon actual performance of the business against pre-agreed limits, for example customer deposit outflows. Others will be based around general or specific market movements.

23. Risk management - liquidity risk (continued)

Liquidity Measurement and Monitoring (continued)
Liquidity risk performance reports are reviewed by ALCO. Any breach or material deterioration of these metrics will set in motion a series of actions and escalations.

The Group's liquidity risk framework is subject to internal oversight, challenge and governance both at Board level and via internal control functions such as Internal Audit. The Group is also subject to regulatory review and challenge.

Stress testing
The strength of any bank's liquidity risk management can only be evaluated based on its ability to survive under stress. The Group evaluates its ability to survive when subjected to simulated stress conditions.

Simulated liquidity stress testing is regularly performed. Stress tests are designed to look at the impact of a variety of firm-specific and market-related scenarios on the adequacy of the Group's liquidity resources at various points in time. Stress tests can therefore be run on an ad hoc basis in response to the emergence of one of these risks.

Scenarios include assumptions about significant changes in key funding sources, external credit ratings, contingent uses of funding and political and economic conditions or events in particular countries. Stress scenarios are applied to both on-balance sheet instruments and off-balance sheet activities to provide a comprehensive view of potential cash flows.

In determining the adequacy of the Group's liquidity resources the Group focuses on the stressed outflows it could anticipate experiencing as a result of any stress scenario occurring. These outflows are measured as occurring over certain time periods which extend from any given day, out to two weeks or to as long as three months. The Group is expected to be able to withstand these stressed outflows through its own resources (principally the use of the liquidity buffer) over these time horizons without having to revert to extraordinary central bank or governmental assistance.

Stress tests are augmented from time to time to reflect firm specific or emerging market risks that could have a material impact on the Group's liquidity position.

The results of stress testing are an active part of management and strategy in balance sheet management and inform allocation, target and limit discussions. In short, limits in the business-as-usual environment are bounded by capacity to satisfy the Group's liquidity needs in the stress environments.

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

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

The Group is part of the RBS Group and receives ongoing capital, funding and liquidity resources which, coupled with other sources of funding and liquidity, enable the Group to meet its obligations as they fall due. Other sources of funding and liquidity include retail, wholesale and central bank liquidity facilities.

23. Risk management - liquidity risk (continued)

Contractual maturity

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

	Group					
2012	0-3 months €m	3-12 months €m	1-3 years €m	3-5 years €m	5-10 years €m	10-20 years €m
Assets by contractual maturity						
Cash and balances at central banks	221	-	-	-	-	-
Loans and advances to banks	4,075	2	4	-	-	-
Total maturing assets	4,296	2	4	-	-	-
Loans and advances to customers	2,560	8,860	5,449	4,110	7,610	12,228
Total assets	**6,856**	**8,862**	**5,453**	**4,110**	**7,610**	**12,228**
Liabilities by contractual maturity						
Deposits by banks	4,854	16	1,412	3	2	-
Debt securities in issue	25	15	4	-	-	-
Subordinated liabilities	-	77	158	-	615	-
Other liabilities	7	22	-	-	-	-
Total maturing liabilities	4,886	130	1,574	3	617	-
Customer accounts	14,012	3,925	1,411	515	165	-
Total liabilities	**18,898**	**4,055**	**2,985**	**518**	**782**	**-**
Maturity gap	**(12,042)**	**4,807**	**2,468**	**3,592**	**6,828**	**12,228**
Cumulative maturity gap	**(12,042)**	**(7,235)**	**(4,767)**	**(1,175)**	**5,653**	**17,881**

	Group					
2011	0-3 months €m	3-12 months €m	1-3 years €m	3-5 years €m	5-10 years €m	10-20 years €m
Assets by contractual maturity						
Cash and balances at central banks	272	-	-	-	-	-
Loans and advances to banks	3,391	-	4	8	-	-
Debt securities	10	-	21	-	-	-
Total maturing assets	3,673	-	25	8	-	-
Loans and advances to customers	4,476	7,712	6,717	4,521	8,631	13,767
Total assets	8,149	7,712	6,742	4,529	8,631	13,767
Liabilities by contractual maturity						
Deposits by banks	12,063	22	201	26	3	-
Debt securities in issue	-	7	17	-	-	-
Subordinated liabilities	5	19	111	168	119	436
Total maturing liabilities	12,068	48	329	194	122	436
Customer accounts	12,593	3,718	1,257	368	168	-
Total liabilities	24,661	3,766	1,586	562	290	436
Maturity gap	(16,512)	3,946	5,156	3,967	8,341	13,331
Cumulative maturity gap	(16,512)	(12,566)	(7,410)	(3,443)	4,898	18,229

23. Risk management - liquidity risk (continued)

Contractual maturity (continued)

	Bank					
2012	0-3 months €m	3-12 months €m	1-3 years €m	3-5 years €m	5-10 years €m	10-20 years €m
Assets by contractual maturity						
Cash and balances at central banks	221	-	-	-	-	-
Loans and advances to banks	3,007	2	4	-	-	-
Debt securities	11,079	-	-	-	-	-
Total maturing assets	14,307	2	4	-	-	-
Loans and advances to customers	5,061	8,860	5,422	4,110	7,634	12,228
Total assets	**19,368**	**8,862**	**5,426**	**4,110**	**7,634**	**12,228**
Liabilities by contractual maturity						
Deposits by banks	4,787	16	1,412	3	2	-
Debt securities in issue	25	15	4	-	-	-
Subordinated liabilities	-	77	158	-	615	-
Other liabilities	7	25	-	-	-	-
Total maturing liabilities	4,819	133	1,574	3	617	-
Customer accounts	30,870	3,925	1,411	517	318	-
Total liabilities	**35,689**	**4,058**	**2,985**	**520**	**935**	**-**
Maturity gap	**(16,321)**	**4,804**	**2,441**	**3,590**	**6,699**	**12,228**
Cumulative maturity gap	**(16,321)**	**(11,517)**	**(9,076)**	**(5,486)**	**1,213**	**13,441**

	Bank					
2011	0-3 months €m	3-12 months €m	1-3 years €m	3-5 years €m	5-10 years €m	10-20 years €m
Assets by contractual maturity						
Cash and balances at central banks	272	-	-	-	-	-
Loans and advances to banks	2,261	-	4	8	-	-
Debt securities	11,852	706	21	-	-	-
Total maturing assets	14,385	706	25	8	-	-
Loans and advances to customers	6,498	7,717	6,729	4,533	8,662	13,829
Total assets	20,883	8,423	6,754	4,541	8,662	13,829
Liabilities by contractual maturity						
Deposits by banks	12,077	22	208	19	3	-
Debt securities in issue	-	7	17	-	-	-
Subordinated liabilities	5	19	111	168	119	436
Total maturing liabilities	12,082	48	336	187	122	436
Customer accounts	16,261	3,718	1,257	368	168	-
Total liabilities	28,343	3,766	1,593	555	290	436
Maturity gap	(7,460)	4,657	5,161	3,986	8,372	13,393
Cumulative maturity gap	(7,460)	(2,803)	2,358	6,344	14,716	28,109

23. Risk management - liquidity risk (continued)

Other contractual cash obligations

	Group					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2012	€m	€m	€m	€m	€m	€m
Operating leases	6	17	44	38	48	22
Contractual obligations to purchase goods or services	1	2	3	-	-	-
	7	**19**	**47**	**38**	**48**	**22**

	Group					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2011	€m	€m	€m	€m	€m	€m
Operating leases	6	19	48	44	75	31
Contractual obligations to purchase goods or services	1	2	3	-	-	-
	7	21	51	44	75	31

	Bank					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2012	€m	€m	€m	€m	€m	€m
Operating leases	6	17	44	38	48	22
Contractual obligations to purchase goods or services	1	2	3	-	-	-
	7	**19**	**47**	**38**	**48**	**22**

	Bank					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2011	€m	€m	€m	€m	€m	€m
Operating leases	6	19	48	44	75	31
Contractual obligations to purchase goods or services	1	2	2	-	-	-
	7	21	50	44	75	31

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

If the repayment of a financial asset or liability is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the asset is included in the latest date on which it can repay regardless of early repayment whereas the liability is included at the earliest possible date that the conditions could be fulfilled without considering the probability of the conditions being met. For example, if a structured note is automatically prepaid 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 in issue 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. As the repayment of assets and liabilities are linked, the repayment of assets in securitisations are shown on the earliest date that the asset can be prepaid as this is the basis used for liabilities.

The principal amounts of financial assets and liabilities that are repayable after 20 years or where the counterparty has no right to repayment of the principal are excluded from the table as are interest payments after 20 years.

23. Risk management (continued)

Credit Risk

Credit risk is the risk of financial loss due to the failure of a customer to meet its obligation to settle outstanding amounts. The credit risk that the Group faces arises mainly from wholesale and retail lending, provision of contingent obligations (such as letters of credit and guarantees) and counterparty credit risk arising from derivative contracts entered into with customers. Other material risks covered by the Group's credit risk management framework are:

- *Concentration risk* - The risk of an outsized loss due to the concentration of credit risk to a specific asset class or product, industry sector, customer or counterparty, or country.
- *Settlement risk* - The intra-day risk that arises where the Group releases funds prior to confirmed receipt of value from a third party.
- *Issuer risk* - The risk of loss on a tradable instrument (e.g. bond, equity or synthetic instrument such as a credit default swap) due to default by the issuer.
- *Wrong way risk* - The risk of loss that arises when the risk factors driving the exposure to a counterparty are positively correlated with the probability of default for that counterparty.
- *Credit mitigation risk* - The risk that credit risk mitigation is not enforceable or that the value of such mitigation decreases, thereby leading to unanticipated losses.

Objectives, organisation and governance
The existence of a strong credit risk management function is vital to support the ongoing profitability of the Group. The potential for loss through economic cycles is mitigated through the embedding of a robust credit risk culture within the business units and through a focus on the importance of sustainable lending practices. The role of the credit risk management function is to own the credit approval, concentration and credit risk control frameworks and to act as the ultimate authority for the approval of credit. This, together with strong independent oversight and challenge, enables the business to maintain a sound lending environment within risk appetite.

Responsibility for development of RBS Group-wide policies, credit risk frameworks, RBS Group-wide portfolio management and assessment of provision adequacy resides with the Group Credit Risk (GCR) function under the management of the Group Chief Risk Officer. Responsibility for application of these policies within the RBS Group resides with the Group Chief Risk Officer.

Ulster Bank Credit Risk ("UBCR") works together with GCR to ensure that the expressed risk appetite is met, within a clearly defined and managed control environment. UBCR operates under the management of the Group Chief Risk Officer.

Material aspects of the Group's credit risk management framework, such as credit risk appetite and limits for portfolios of strategic significance, are considered and approved by the Executive Risk Forum (ERF). The ERF has delegated authority to the Group Credit Risk Committee, a functional sub-committee of Group Risk Committee, to act on credit risk matters. These include, but are not limited to, credit risk appetite and limits (within the overall risk appetite set by the Board and the ERF), credit risk strategy and frameworks, credit risk policy and the oversight of the credit profile across the Group.

Credit risk management framework
The Group has established an appropriate and comprehensive framework for the management of credit risk that includes governance structures, risk appetite and concentration frameworks, policies, measurement and reporting tools and independent assurance.

In order to strengthen this framework and ensure consistent application, risk appetite statements and a set of credit control standards were launched to supplement the existing policy suite. These standards address divisional governance and policy requirements and reflect a set of behavioural, organisational and management norms that will drive a sound control environment and embed a strong risk culture.

Risk appetite and concentration risk management
Risk appetite has been expressed by the Board through the setting of specific quantitative risk appetite targets under stress. Of particular relevance in the management of credit risk are the targets for earnings volatility and capital adequacy. The Group's credit risk framework has therefore been designed around the factors that influence the Group's ability to meet these targets. These include the limiting of excess credit risk concentrations which generate higher volatility under stress and, if not adequately controlled, can undermine capital adequacy.

The Group's credit concentration frameworks are designed to limit concentration by product/asset class, industry sector, customer or counterparty (i.e. single name) and country. The frameworks are supported by a suite of policies that set out the risk parameters within which business units may operate.

23. Risk management - credit risk (continued)

Risk appetite and concentration risk management (continued)
The management of concentration risk and associated limits are now firmly embedded in the risk management processes of the Group and form a pivotal part of the Risk function's engagement with the businesses on the appropriateness of risk appetite choices. In the three years since the new concentration frameworks were rolled out across the Group, UBCR has reviewed all material industry and product portfolios and agreed a risk appetite commensurate with the franchises represented in these reviews. In particular, limits have been reviewed and re-sized, to refine the Group's risk appetite in areas where it faces significant balance sheet concentrations or franchise challenges.

Notwithstanding the need for the Group to control credit risk volatility, the Group's businesses and credit functions pay careful consideration to the need to ensure sufficient capacity within credit limits to support customers of sound credit quality, in particular within retail and small business customer segments.

During 2012, the Group expanded the scope of its credit risk appetite controls through the active management of non-financial risks in the Group's lending decisions. The development of Environmental, Social and Ethical (ESE) risk policies for sectors considered to present a higher reputational risk allow the Group to manage its reputational risks. The policies set the Group's reputational risk appetite for clients operating in higher-risk sectors and help to shape wider sector management strategies. The ESE framework forms part of a wider initiative by the Group to improve reputational risk management and build trust with its stakeholders (for more information on reputational risk management, refer to page 74).

Product/asset class
- *Retail* - A formal framework establishes Group-level statements and thresholds that are cascaded to all business lines. These include measures that relate both to aggregate portfolios and to asset quality at origination, which are tracked frequently to ensure consistency with Group standards and appetite. This appetite setting and tracking then informs the processes and parameters employed in origination activities, which require a large volume of small-scale credit decisions, particularly those involving an application for a new product or a change in facilities on an existing product. The majority of these decisions are based upon automated strategies utilising credit and behaviour scoring techniques. Scores and strategies are typically segmented by product, brand and other significant drivers of credit risk. These data-driven strategies utilise a wide range of credit information relating to a customer including, where appropriate, information across customer holdings. A small number of credit decisions are subject to additional manual underwriting by authorised approvers in specialist units. These include higher-value, more complex, small business and personal unsecured transactions and some residential mortgage applications.

- *Wholesale* - Formal policies, specialised tools and expertise, tailored monitoring and reporting and, in certain cases, specific limits and thresholds are deployed to address certain lines of business across the Group, where the nature of credit risk incurred could represent a concentration or a specific/heightened risk in some other form. Those portfolios identified as potentially representing a concentration or heightened risk are subject to formal governance, including periodic review.

Sector concentration
Across wholesale portfolios, exposures are assigned to, and reviewed in the context of, a defined set of industry sectors. Through this sector framework, appetite and portfolio strategies are agreed and set at aggregate and more granular levels, where exposures have the potential to represent excessive concentration or where trends in both external factors and internal portfolio performance give cause for concern. Formal periodic reviews are undertaken, depending on materiality, these may include an assessment of the Group's franchise in a particular sector, an analysis of the outlook (including downside outcomes), identification of key vulnerabilities and stress/scenario tests.

The focus during 2012 was on embedding sector and sub-sector specific appetite and on setting appropriate controls. This includes strengthening portfolio controls on key metrics and lending parameters, and the ongoing development of sector-specific lending policies.

Single-name concentration
Within wholesale portfolios, much of the activity undertaken by the credit risk function is organised around the assessment, approval and management of the credit risk associated with a borrower or group of related borrowers.

A formal single name concentration framework addresses the risk of outsized exposure to a borrower or borrower group. The framework includes specific and sometimes elevated approval requirements, additional reporting and monitoring, and the requirement to develop plans to address and reduce excess exposures over an appropriate timeframe.

23. Risk management - credit risk (continued)

Single-name concentration (continued)
Credit approval authority is discharged by way of a framework of individual delegated authorities, which requires at least two individuals to approve each credit decision, one from the business and one from the credit risk management function. Both parties must hold sufficient delegated authority under the Group-wide authority grid. While both parties are accountable for the quality of each decision taken, the credit risk management approver holds ultimate sanctioning authority. The level of authority granted to individuals is dependent on their experience and expertise, with only a small number of senior executives holding the highest authority provided under the framework. Daily monitoring of individual counterparty limits is undertaken.

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; and compliance with terms and conditions. For certain counterparties, early warning indicators are also in place to detect deteriorating trends in limit utilisation or account performance, and to prompt additional oversight.

Since 2009, the Group has been managing its corporate exposures to reduce concentrations and align its appetite for future business to the Group's broader strategies for its large corporate franchises. The Group is continually reviewing its single name concentration framework to ensure that it remains appropriate for current economic conditions and in line with improvements in the Group's risk measurement models.

In 2012, the Group implemented further refinements to the single name exposure management controls already in place, which brings them more closely in line with market best practice and which allows the Group to differentiate more consistently between the different risk types.

Global Restructuring Group (GRG)

GRG manages problem and potential problem exposures in the Group's wholesale credit portfolios. Its primary function is to actively manage the exposures to minimise loss for the Group and, where feasible, to return the exposure to the Group's mainstream loan book.

Originating business units consult with GRG prior to transferring exposures to it when a potentially negative event or trend emerges that might affect a customer's ability to service its debt or increase the Group's risk exposure to that customer. Such circumstances include deteriorating trading performance, likely breach of covenant, challenging macroeconomic conditions, a missed payment or the expectation of a missed payment to the Group or another creditor.

On transfer of the relationship, GRG aim to devise a bespoke strategy that optimises recoveries from the debt. This strategy may also involve GRG reviewing the business operations and performance of the customer. A number of alternative approaches will typically be considered including:

- *Covenant relief:* the temporary waiver or recalibration of covenants may be granted to mitigate a potential or actual covenant breach. Such relief is usually granted in exchange for fees, increased margin, additional security, or a reduction in maturity profile of the original loan.
- *Amendment of restrictive covenants:* restrictions in loan documents may be amended or waived as part of an overall remedial strategy to allow: additional indebtedness; the granting of collateral; the sale of a business; the granting of junior lien on the collateral; or other fundamental change in capital or operating structure of the enterprise.
- *Variation in margin:* contractual margin may be amended to bolster the customer's day-to-day liquidity, with the aim of helping to sustain the customer's business as a going concern. This would normally be accompanied by the Group receiving an exit payment, payment in kind or deferred fee.
- *Payment holidays and loan rescheduling:* payment holidays or changes to the contracted amortisation profile including extensions in contracted maturity or roll-overs may be granted to improve customer liquidity. Such concessions often depend on the expectation that liquidity will recover when market conditions improve or from capital raising initiatives that access alternative sources of liquidity. Recently, these types of concessions have become more common in commercial real estate transactions in situations when a shortage of market liquidity rules out immediate refinancing and makes short-term forced collateral sales unattractive.
- *Forgiveness of all or part of the outstanding debt:* debt may be forgiven or exchanged for equity where a fundamental shift in the customer's business or economic environment means that other forms of restructuring strategies are unlikely to succeed in isolation and the customer is incapable of servicing current debt obligations. Debt forgiveness is often an element in leveraged finance transactions which are typically structured on the basis of projected cash flows from operational activities rather than underlying tangible asset values. Maintaining the business as a going concern with a sustainable level of debt is the preferred option rather than realising value of the underlying assets, provided that the underlying business model and strategy are considered viable.

23. Risk management – credit risk (continued)

Global Restructuring Group (continued)

Depending on the case in question, GRG may employ a combination of these options in order to achieve the best outcome. It may also consider alternative approaches, either alone or together with the options listed above.

The following are generally considered as options of last resort:

- *Examinership:* in a limited number of cases the option of examinership may prove to be effective in delivering a restructuring under the protection of the courts where a decision of multiple creditor groups is required.
- *Enforcement of security or otherwise taking control of assets:* where the Group holds underlying collateral or other security interest and is entitled to enforce its rights, it may take ownership or control of the assets. The Group's preferred strategy is to consider other possible options prior to exercising these rights.
- *Insolvency:* where there is no suitable restructuring option or the business is no longer regarded as 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.

As discussed above, GRG will consider a range of possible restructuring strategies. At the time of execution, the ultimate outcome of the strategy adopted is unknown and highly dependent on the cooperation of the borrower and the continued existence of a viable business. The customer's financial position, its anticipated future prospects and the likely effect of the restructuring including any concessions are considered by the GRG relationship manager to establish whether an impairment provision is required, subject to divisional and Group governance.

Retail collections and recoveries

There are collections and recoveries functions in each of the consumer businesses. Their role is to provide support and assistance to customers who are currently experiencing difficulties meeting their financial obligations. Where possible, the aim of the collections and recoveries teams is to return the customer to a satisfactory position, by working with them to restructure their finances. If this is not possible, the team has the objective of reducing the loss to the Group.

Forbearance

Within the Group's retail businesses, forbearance generally occurs when the business, for reasons relating to the actual or potential financial stress of a borrower, grants a permanent or temporary concession to that borrower. Forbearance is granted principally to customers with mortgages. Granting of forbearance to unsecured customers is less extensive.

Mortgage Arrears Resolution Strategies ("MARS") is a CBI sponsored initiative for all banks in the Republic of Ireland that aims to increase the level of engagement and options available to mortgage customers in financial difficulty. The Bank started to develop new MARS contact strategies and treatments in September 2011 and presented for approval to Board in October 2012. The MARS strategies went live in December 2012.

Identification of forbearance
Mortgages are identified for forbearance treatment following initial contact from the customer, in the event of payment arrears or when the customer is transferred to collections or recoveries.

Forbearance is granted following an assessment of the customer's ability to pay. Customers receiving these types of treatment whilst in collections or recoveries are typically showing signs of financial difficulties. Within the Group, requests by customers for an amendment to their contractual terms whilst they are fully up-to-date with payments are considered to be a potential impairment indicator.

Types of retail forbearance
A number of forbearance options are utilised by the Group's retail businesses. These include, but are not limited to, reduced repayments, payment holidays, capitalisation of arrears, term extensions and temporary conversions to interest only.

For those loans classified as non-performing, the Group's objective in granting forbearance is to minimise the loss on these accounts and, wherever possible, return the customer to a performing state. The Group's aim is to enable customers who are current on their payments to continue to service the loan.

The mortgage forbearance population is reviewed regularly to ensure that customers are meeting the agreed terms of the arrangement. Key metrics have been developed to record the proportion of customers who fail to meet the agreed terms over time as well as the proportion of customers who return to a performing state with no arrears.

23. Risk management - credit risk (continued)

Forbearance (continued)

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

	2012		2011	
	Balance	**Provisions**	Balance	Provisions
Arrears status and provisions	**€m**	**€m**	€m	€m
No missed payments	**1,066**	**118**	1,051	92
1-3 months in arrears	**642**	**71**	609	53
>3 months in arrears	**630**	**232**	500	148
Total	**2,338**	**421**	2,160	293

The incidence of the main types of retail forbearance on the balance sheet as at 31 December 2012 is analysed below. Definitions are based on those used within the CBI and FSA forbearance guidelines. For a small proportion of mortgages, more than one forbearance type applies.

	2012	2011
	€m	€m
Interest only	**1,090**	944
Term extensions – capital repayment & interest only	**215**	68
Payment concession/holidays	**892**	1,029
Capitalisation of arrears	**141**	119
Total	**2,338**	2,160
% of total mortgage stock	**10.5%**	10.1%

Provisioning for retail customers

Provisions are assessed in accordance with the Group's provisioning policies which comply with IAS 39 'Financial Instruments: Recognition and Measurement'. For the non-performing population, a collective assessment is made. Within the performing book, latent loss provisions are held for those loans that are impaired but not yet identified.

The majority of mortgage accounts subject to forbearance remains in the performing book but these accounts are identified and monitored separately from other performing accounts. They are subject to higher provisioning rates than the remainder of the performing book (currently approximately eight times higher). These rates are reviewed monthly. Once forbearance is granted, the account continues to be assessed separately for latent provisioning until the forbearance period expires. After that point, the account is no longer separately identified for latent provisioning. Non-performing mortgage accounts that have been granted forbearance carry the same provision rate as non-forborne accounts.

Controls and assurance

The Group's credit control and assurance framework comprises three key components: credit policy, policy compliance assurance and independent assurance.

The foundation is the RBS Group Credit Policy Standard, which as part of the Group Policy Framework ("GPF"), sets out the rules the Group's businesses must follow to ensure that credit risks are identified and effectively managed through the credit lifecycle. During 2012, a major revision of the RBS Group's key credit policies was completed. This revision has provided support in ensuring that the Group's control environment is appropriately aligned to the approved risk appetite, and provides a sound basis for the Group's independent audit and assurance activities across the credit risk function.

The second component is a policy assurance activity that GCR undertakes to provide the Group Chief Credit Officer with evidence of the effectiveness of the controls in place across the Group to manage credit risk. The results of these reviews are presented to the Group Credit Risk Committee on a regular basis in support of the self-certification that GCR is obliged to complete under the GPF.

Lastly, a strong independent assurance function is an important element of a sound control environment. During 2011, the RBS Group took the decision to strengthen its Credit Quality Assurance (CQA) activities and moved all divisional CQA resources under the centralised management of GCR. The benefits of this action are already apparent in greater consistency of standards and cross-utilisation of resources, ensuring that subject matter experts bring their expertise to bear where relevant.

23. Risk management - credit risk (continued)

Provisioning for retail customers (continued)

Controls and assurance (continued)
Reviews undertaken consistently address the four underlying risk pillars of: risk management, risk appetite, ratings and data integrity, and asset quality. Appropriate identification, escalation, remediation and related tracking of control breaches and improvements in operational processes are firmly embedded in the assurance process to ensure that divisions act upon review findings.

Credit risk measurement
Credit risk models are used throughout the Group to support the quantitative risk assessment element within the credit approval process, ongoing credit risk management, monitoring and reporting and portfolio analytics.

The Group is undertaking a significant programme of updates and improvements to its Wholesale credit risk models, including the incorporation of more recent data and reflecting updated regulatory requirements applying to some aspects of Wholesale Internal Ratings Based (IRB) modelling. Material updates to certain models, notably those used in Sovereign and Financial Institution asset classes, have been implemented during 2012 and are reflected in measures of risk reported in the Group's disclosures. Further updates, primarily in the Corporate asset class, are planned for 2013.

The model updates are generally in segments of the portfolio where risk experience has remained limited even in recent periods and primarily result in increases to measures that still remain within ranges representing lower risk business relative to the Group's broader risk profile; in terms of Probability of Default models, for example, the changes occur largely within ranges equivalent to Investment Grade ratings.

Material aspects of these changes have been anticipated in risk frameworks and in other areas that are dependent on these measures, notably including the Group's Risk Appetite framework. In some portfolios the anticipated impact on Risk Weighted Assets has been realised, as part of a process defined with regulators, prior to introduction of the updated models.

These models assess the probability that a customer will fail to make full and timely repayment of its obligations. The probability of a customer failing to do so is measured over a one year period through the economic cycle, although certain retail scorecards use longer periods for business management purposes.

Wholesale businesses - As part of the credit assessment process, each counterparty is assigned an internal credit grade derived from a default probability. There are a number of different credit grading models in use across the Group, each of which considers risk characteristics particular to that type of customer. The credit grading modules score a combination of quantitative inputs (for example recent financial performance) and qualitative inputs (for example management performance of sector outlook).

Retail businesses - Each customer account is separately scored using models based on the most material drivers of default. In general, scorecards are statistically derived using customer data. Customers are assigned a score, which in turn is mapped to a probability of default. The probabilities of default are used to support automated credit decision making and to group customers into risk pools for regulatory capital calculations.

Exposure at default
Facility usage models estimate the expected level of utilisation of a credit facility at the time of a borrower's default. For revolving and variable draw-down type products which are not fully drawn, the exposure at default (EAD) will typically be higher than the current utilisation. The methodologies used in EAD modelling provide an estimate of potential exposure and recognise that customers may make more use of their existing credit facilities as they approach default.

Counterparty credit risk exposure measurement models are used for derivatives and other traded instruments, where the amount of credit risk exposure may be dependent upon one or more underlying market variables, such as interest or foreign exchange rates. These models drive internal credit risk management activities such as limit and excess management.

Loss given default
These models estimate the economic loss that may be experienced (the amount that cannot be recovered) by the Group on a credit facility in the event of default. The Group's loss given default models take into account both borrower and facility characteristics for unsecured or partially unsecured facilities, as well as the quality of any risk mitigation that may be in place for secured facilities, the cost of collections and a time discount factor for the delay in cash recovery.

23. Risk management - credit risk (continued)

Credit risk assets

In the tables and commentary below, exposure refers to credit risk assets, which consist of:

- *Lending* - Comprises gross loans and advances to: central and local governments; central banks, including cash balances; other banks and financial institutions, incorporating overdraft and other short-term credit lines; corporations, in large part loans and leases; and individuals, comprising mortgages, personal loans and credit card balances. Lending includes both impaired loans and those loans where an impairment event has taken place, but no impairment provision is recognised.
- *Derivatives* - Comprises the mark-to-market (mtm) value of such contracts after the effect of enforceable netting agreements, but before the effect of collateral. In the event of a counterparty default, this is the amount due from the counterparty. Figures shown apply counterparty netting within the regulatory capital model used.
- *Contingent obligations* - Comprises primarily letters of credit and guarantees.

Credit risk assets exclude issuer risk (primarily debt securities) and reverse repurchase arrangements. They take account of legal netting arrangements that provide a right of legal set-off, but do not meet the offset criteria under IFRS.

Asset quality

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

The table below shows credit risk assets by asset quality (AQ) band:

Asset Quality Grade	Minimum	Maximum
AQ1	0.000	0.034
AQ2	0.034	0.048
AQ3	0.048	0.095
AQ4	0.095	0.381
AQ5	0.381	1.076
AQ6	1.076	2.153
AQ7	2.153	6.089
AQ8	6.089	17.222
AQ9	17.222	100.000
AQ10	100.000	100.000

The following table provides an analysis of the credit quality of third party financial assets by probability of default.

	Group					
2012	Cash and balances at central banks €m	Loans and advances to banks €m	Loans and advances to customers €m	Derivatives €m	Commitments €m	Contingent liabilities €m
AQ1	221	4,010	820	591	144	1
AQ2	-	1	17	49	180	57
AQ3	-	3	80	47	22	39
AQ4	-	67	771	52	844	139
AQ5	-	1	866	6	232	29
AQ6	-	-	4,497	3	461	60
AQ7	-	-	9,832	8	350	61
AQ8	-	-	2,166	82	127	53
AQ9	-	-	5,110	144	60	10
AQ10	-	-	-	1	349	77
Accruing past due	-	-	3,211	-	-	-
Non-accrual	-	-	18,521	-	-	-
Impairment provisions	-	-	(10,715)	-	-	-
Total	**221**	**4,082**	**35,176**	**983**	**2,769**	**526**

23. Risk management - credit risk (continued)

Asset quality (continued)

Group						
2011	Cash and balances at central banks €m	Loans and advances to banks €m	Loans and advances to customers €m	Derivatives €m	Commitments €m	Contingent liabilities €m
AQ1	272	3,366	924	876	295	52
AQ2	-	-	72	13	140	41
AQ3	-	-	250	45	218	39
AQ4	-	26	528	12	480	125
AQ5	-	-	1,849	23	370	40
AQ6	-	1	6,861	8	489	108
AQ7	-	11	10,284	35	307	88
AQ8	-	-	2,340	106	143	14
AQ9	-	-	5,279	127	72	27
AQ10	-	-	-	-	333	117
Accruing past due	-	-	2,972	-	-	-
Non-accrual	-	-	16,288	-	-	-
Impairment provisions	-	-	(8,634)	-	-	-
Total	272	3,404	39,013	1,245	2,847	651

Bank						
2012	Cash and balances at central banks €m	Loans and advances to banks €m	Loans and advances to customers €m	Derivatives €m	Commitments €m	Contingent liabilities €m
AQ1	221	2,941	3,319	588	144	1
AQ2	-	1	17	49	180	57
AQ3	-	3	80	47	22	39
AQ4	-	67	771	52	844	139
AQ5	-	1	866	6	232	29
AQ6	-	-	4,497	3	461	60
AQ7	-	-	9,830	8	350	61
AQ8	-	-	2,166	82	127	53
AQ9	-	-	5,110	144	60	10
AQ10	-	-	-	1	349	77
Accruing past due	-	-	3,211	-	-	-
Non-accrual	-	-	18,521	-	-	-
Impairment provisions	-	-	(10,715)	-	-	-
Total	**221**	**3,013**	**37,673**	**980**	**2,769**	**526**

Bank						
2011	Cash and balances at central banks €m	Loans and advances to banks €m	Loans and advances to customers €m	Derivatives €m	Commitments €m	Contingent liabilities €m
AQ1	272	2,236	3,188	756	295	52
AQ2	-	-	72	13	140	41
AQ3	-	-	250	45	218	39
AQ4	-	26	528	12	480	125
AQ5	-	-	1,849	23	370	40
AQ6	-	1	6,861	8	489	108
AQ7	-	11	10,284	35	307	88
AQ8	-	-	2,340	106	143	14
AQ9	-	-	5,279	127	72	27
AQ10	-	-	-	-	333	117
Accruing past due	-	-	2,972	-	-	-
Non-accrual	-	-	16,288	-	-	-
Impairment provisions	-	-	(8,634)	-	-	-
Total	272	2,274	41,277	1,125	2,847	651

Loans and advances to customers, past due at balance sheet date but not considered impaired are shown in Note 9.

23. Risk management - credit risk (continued)

Credit risk assets by industry and geography

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

	Group				
2012	Gross loans and advances to banks and customers €m	Debt securities and equity shares €m	Derivatives €m	Total €m	Netting and offset [1] €m
UK					
Manufacturing	94	-	1	**95**	-
Construction	6	-	-	**6**	-
Finance	5	-	114	**119**	-
Service industries and business activities	124	-	20	**144**	-
Property	1,854	-	52	**1,906**	-
Individuals					
Home mortgages	-	-	-	**-**	-
Other	2	-	-	**2**	-
Interest accruals	1	-	-	**1**	-
Total UK	**2,086**	**-**	**187**	**2,273**	**-**
Rest of Europe [2]					
Central and local government	51	-	-	**51**	-
Manufacturing	773	-	20	**793**	10
Construction	625	-	-	**625**	25
Finance	4,841	8	598	**5,447**	-
Service industries and business activities	5,904	-	79	**5,983**	73
Agriculture, forestry and fishing	863	-	1	**864**	36
Property	12,981	-	98	**13,079**	6
Individuals					
Home mortgages	20,707	-	-	**20,707**	1
Other	1,108	-	-	**1,108**	-
Interest accruals	34	-	-	**34**	-
Total Rest of Europe	**47,887**	**8**	**796**	**48,691**	**151**
Total					
Central and local government	51	-	-	**51**	-
Manufacturing	867	-	21	**888**	10
Construction	631	-	-	**631**	25
Finance	4,846	8	712	**5,566**	-
Service industries and business activities	6,028	-	99	**6,127**	73
Agriculture, forestry and fishing	863	-	1	**864**	36
Property	14,835	-	150	**14,985**	6
Individuals					
Home mortgages	20,707	-	-	**20,707**	1
Other	1,110	-	-	**1,110**	-
Interest accruals	35	-	-	**35**	-
	49,973	**8**	**983**	**50,964**	**151**

(1) This column shows the amount by which the Group's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Group a legal right to set-off the financial asset against a financial liability due to the same counterparty. In addition, the Group holds collateral in respect of 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 receivables; 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.

(2) Rest of Europe balances relate predominantly to the Republic of Ireland.

ULSTER BANK IRELAND LIMITED

NOTES TO THE FINANCIAL STATEMENTS *for the year ended 31 December 2012*

23. Risk management - credit risk (continued)

Credit risk assets by industry and geography (continued)

	Group				
2011	Gross loans and advances to banks and customers €m[1]	Debt securities and equity shares €m	Derivatives €m	Total €m	Netting and offset [2] €m
UK					
Manufacturing	120	-	1	121	-
Construction	7	-	-	7	
Finance	14	-	3	17	-
Service industries and business activities	118	-	22	140	-
Agriculture, forestry and fishing	-	-	2	2	-
Property	1,936	-	64	2,000	-
Individuals					
Other	1	-	-	1	
Interest accruals	4	-	-	4	-
Total UK	2,200	-	92	2,292	-
Rest of Europe [3]					
Central and local government	53	-	-	53	-
Manufacturing	839	-	13	852	11
Construction	640	-	-	640	29
Finance	4,043	38	920	5,001	1
Service industries and business activities	6,127	-	80	6,207	82
Agriculture, forestry and fishing	832	-	-	832	37
Property	13,828	-	140	13,968	11
Individuals					
Home mortgages	21,250	-	-	21,250	-
Other	1,175	-	-	1,175	-
Interest accruals	64	-	-	64	-
Total Rest of Europe	48,851	38	1,153	50,042	171
Total					
Central and local government	53	-	-	53	-
Manufacturing	959	-	14	973	11
Construction	647	-	-	647	29
Finance	4,057	38	923	5,018	1
Service industries and business activities	6,245	-	102	6,347	82
Agriculture, forestry and fishing	832	-	2	834	37
Property	15,764	-	204	15,968	11
Individuals					
Home mortgages	21,250	-	-	21,250	-
Other	1,176	-	-	1,176	-
Interest accruals	68	-	-	68	-
	51,051	38	1,245	52,334	171

(1) 2011 Gross loans and advances to customers have been reclassified to better reflect the geographical split of balances.

(2) This column shows the amount by which the Group's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Group a legal right to set-off the financial asset against a financial liability due to the same counterparty. In addition, the Group holds collateral in respect of 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 receivables; 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.

(3) Rest of Europe balances relate predominantly to the Republic of Ireland.

23. Risk management - credit risk (continued)

Credit risk assets by industry and geography (continued)

	Bank				
2012	Gross loans and advances to banks and customers €m	Debt securities and equity shares €m	Derivatives €m	Total €m	Netting and offset [1] €m
UK					
Manufacturing	94	-	1	**95**	-
Construction	6	-	-	**6**	-
Finance	5	-	42	**47**	-
Service industries and business activities	124	-	19	**143**	-
Property	1,854	-	70	**1,924**	-
Individuals					
Home mortgages	-	-	-	**-**	-
Other	2	-	-	**2**	-
Interest accruals	1	-	-	**1**	-
Total UK	**2,086**	**-**	**132**	**2,218**	**-**
Rest of Europe [2]					
Central and local government	51	-	-	**51**	-
Manufacturing	771	-	21	**792**	10
Construction	624	-	-	**624**	25
Finance	6,276	11,087	645	**18,008**	-
Service industries and business activities	5,903	-	86	**5,989**	73
Agriculture, forestry and fishing	863	-	1	**864**	36
Property	12,980	-	95	**13,075**	6
Individuals					
Home mortgages	20,707	-	-	**20,707**	1
Other	1,106	-	-	**1,106**	-
Interest accruals	34	-	-	**34**	-
Total Rest of Europe	**49,315**	**11,087**	**848**	**61,250**	**151**
Total					
Central and local government	51	-	-	**51**	-
Manufacturing	865	-	22	**887**	10
Construction	630	-	-	**630**	25
Finance	6,281	11,087	687	**18,055**	-
Service industries and business activities	6,027	-	105	**6,132**	73
Agriculture, forestry and fishing	863	-	1	**864**	36
Property	14,834	-	165	**14,999**	6
Individuals					
Home mortgages	20,707	-	-	**20,707**	1
Other	1,108	-	-	**1,108**	-
Interest accruals	35	-	-	**35**	-
	51,401	**11,087**	**980**	**63,468**	**151**

(1) This column shows the amount by which the Group's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Group a legal right to set-off the financial asset against a financial liability due to the same counterparty. In addition, the Group holds collateral in respect of 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 receivables; 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.

(2) Rest of Europe balances relate predominantly to the Republic of Ireland.

ULSTER BANK IRELAND LIMITED

23. Risk management - credit risk (continued)

Credit risk assets by industry and geography (continued)

	Bank				
2011	Gross loans and advances to banks and customers €m[1]	Debt securities and equity shares €m	Derivatives €m	Total €m	Netting and offset [2] €m
UK					
Manufacturing	120	-	1	121	-
Construction	7	-	-	7	-
Finance	14	-	3	17	-
Service industries and business activities	118	-	22	140	-
Agriculture, forestry and fishing	-	-	2	2	-
Property	1,936	-	64	2,000	-
Individuals					
Other	2	-	-	2	-
Interest accruals	4	-	-	4	-
Total UK	2,201	-	92	2,293	-
Rest of Europe [3]					
Central and local government	53	-	-	53	-
Manufacturing	838	-	13	851	11
Construction	639	-	-	639	29
Finance	5,178	12,586	800	18,564	1
Service industries and business activities	6,127	-	80	6,207	82
Agriculture, forestry and fishing	831	-	-	831	37
Property	13,831	-	140	13,971	11
Individuals					
Home mortgages	21,250	-	-	21,250	-
Other	1,174	-	-	1,174	-
Interest accruals	63	-	-	63	-
Total Rest of Europe	49,984	12,586	1,033	63,603	171
Total					
Central and local government	53	-	-	53	-
Manufacturing	958	-	14	972	11
Construction	646	-	-	646	29
Finance	5,192	12,586	803	18,581	1
Service industries and business activities	6,245	-	102	6,347	82
Agriculture, forestry and fishing	831	-	2	833	37
Property	15,767	-	204	15,971	11
Individuals					
Home mortgages	21,250	-	-	21,250	-
Other	1,176	-	-	1,176	-
Interest accruals	67	-	-	67	-
	52,185	12,586	1,125	65,896	171

(1) 2011 Gross loans and advances to customers have been reclassified to better reflect the geographical split of balances.

(2) This column shows the amount by which the Group's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Group a legal right to set-off the financial asset against a financial liability due to the same counterparty. In addition, the Group holds collateral in respect of 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 receivables; 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.

(3) Rest of Europe balances relate predominantly to the Republic of Ireland.

23. Risk management – credit risk (continued)

Credit risk mitigation

Approaches and methodologies

The Group employs a number of structures and techniques to mitigate credit risk. Netting of debtor and creditor balances is undertaken in accordance with relevant regulatory and internal policies. Exposure on over-the-counter derivative and secured financing transactions is further mitigated by the exchange of financial collateral and the use of market standard documentation. Further mitigation may be undertaken in a range of transactions, from retail mortgage lending to large wholesale financing. This 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. Such techniques are used in the management of credit portfolios, typically to mitigate credit concentrations in relation to an individual obligor, a borrower group or a collection of related borrowers.

The use and approach to credit risk mitigation varies by product type, customer and business strategy. Minimum standards applied across the Group cover:

- The suitability of qualifying credit risk mitigation types and any conditions or restrictions applicable to those mitigants;
- The means by which legal certainty is to be established, including required documentation, supportive independent legal opinions and all necessary steps required to establish legal rights;
- Acceptable methodologies for initial and any subsequent valuations of collateral and the frequency with which collateral is to be revalued and the use of collateral haircuts;
- Actions to be taken in the event that the value of mitigation falls below required levels;
- Management of the risk of correlation between changes in the credit risk of the customer and the value of credit risk mitigation;
- Management of concentration risks, for example, by setting thresholds and controls on the acceptability of credit risk mitigants and on lines of business that are characterised by a specific collateral type or structure; and
- Collateral management to ensure that credit risk mitigation remains legally effective and enforceable.

Secured portfolios

Within its secured portfolios, the Group has recourse to various types of collateral and other credit enhancements to mitigate credit risk and reduce the loss to the Group arising from the failure of a customer to meet its obligations. These include: cash deposits; charges over residential and commercial property, debt securities and equity shares; and third-party guarantees. The existence of collateral may affect the pricing of a facility and its regulatory capital requirement. When a collateralised financial asset becomes impaired, the impairment charge directly reflects the realisable value of collateral and any other credit enhancements.

Corporate exposures

The type of collateral taken by the Group's commercial and corporate businesses and the manner in which it is taken will vary according to the activity and assets of the customer.

- *Physical assets* - These include business assets such as stock, plant and machinery, vehicles, ships and aircraft. In general, physical assets qualify as collateral only if they can be unambiguously identified, located or traced, and segregated from uncharged assets. Assets are valued on a number of bases according to the type of security that is granted.
- *Real estate* - The Group takes collateral in the form of real estate, which includes residential and commercial properties. The loan amount will typically exceed the market value of the collateral at origination date. The market value is defined as the estimated amount for which the asset could be sold in an arms length transaction by a willing seller to a willing buyer.
- *Receivables* - When taking a charge over receivables, the Group assesses their nature and quality and the borrower's management and collection processes. The value of the receivables offered as collateral will typically be adjusted to exclude receivables that are past their due dates.

The security charges may be floating or fixed, with the type of security likely to impact: (i) the credit decision; and (ii) the potential loss upon default. In the case of a general charge such as a mortgage debenture, balance sheet information may be used as a proxy for market value if the information is deemed reliable.

23. Risk management – credit risk (continued)

Corporate exposures (continued)
The Group does not recognise certain asset classes as collateral: for example, short leasehold property and equity shares of the borrowing company. Collateral whose value is correlated to that of the obligor is assessed on a case-by-case basis and, where necessary, over-collateralisation may be required.

The Group uses industry-standard loan and security documentation wherever possible. Non-standard documentation is typically prepared by external lawyers on a case-by-case basis. The Group's business and credit teams are supported by in-house specialist documentation teams.

The existence of collateral has an impact on provisioning. Where the Group no longer expects to recover the principal and interest due on a loan in full or in accordance with the original terms and conditions, it is assessed for impairment. If exposures are secured, the current net realisable value of the collateral will be taken into account when assessing the need for a provision. No impairment provision is recognised in cases where all amounts due are expected to be settled in full on realisation of the security.

Residential Mortgages

At 31 December 2012 the Group residential mortgage portfolio totalled €20.7bn which represents a decline of 1% from €20.9bn at 31 December 2011.

The table below shows how the steep property value correction has affected the distribution of residential mortgages by loan-to-value (LTV) (indexed). LTV is based upon gross loan amounts and, whilst including defaulted loans, does not account for impairments already taken.

	Group	
	2012	2011
Residential mortgages – distribution by average LTV (1) indexed	%	%
<=50%	**37.5**	38.9
>50% and <=60%	**5.1**	5.4
>60% and <=70%	**5.0**	5.1
>70% and <=80%	**5.1**	5.2
>80% and <=90%	**5.3**	5.2
>90% and <=100%	**5.0**	5.2
>100%	**37.0**	35.0
Total portfolio average LTV at 31 December	**86.9**	82.8
Average LTV on new originations during the year	**75.8**	67.7

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

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

	Group	
	2012	2011
Personal	%	%
Mortgages	**15.0**	10.3

Collateral and other credit enhancements received

Due to the challenging economic conditions a substantial proportion of the Commercial Real Estate portfolio is in excess of 100% LTV ("REIL"). The market conditions make it extremely challenging to obtain appropriate market valuations and there can be significant differences in values based on geographic location and asset type. Consequently, 70% (€10.4bn) (2011: 70% (€11.2bn)) of the Commercial Real Estate portfolio is actively managed by Non Core of which €9.5bn is categorised REIL with a provision coverage of 59%.

	2012		2011	
Non-performing corporate loans (excluding commercial real estate)	**Loans €m**	**Provisions €m**	Loans €m	Provisions €m
Secured	**410**	**226**	2,521	1,148
Unsecured	**3,356**	**1,487**	638	485

In the year to 31 December 2012 the guidelines determining which balances are considered as secured debt were made more stringent. This has resulted in a significant increase in balances which are classified as unsecured.

23. Risk management – credit risk (continued)

Retail exposures

All borrowing applications, whether secured or not, are subject to appropriate credit risk underwriting processes including affordability assessments. Pricing is typically higher on unsecured than secured loans. For secured loans, pricing will typically vary by LTV: higher-LTV products are typically subject to higher interest rates commensurate with the associated risk.

The value of a property intended to secure a mortgage is assessed during the loan underwriting process using industry-standard methodologies. Property values supporting home equity lending reflect either an individual appraisal or valuations generated by statistically valid automated valuation models. Property values are updated each quarter using the Central Statistics Office Residential Property Price Index.

The existence of collateral has an impact on provisioning levels. Once a secured loan is classified as non-performing, the present realisable value of the underlying collateral and the costs associated with repossession are used to estimate the provision required.

The tables below shows period-end weighted LTVs for the Group's residential mortgage portfolio split between performing and non-performing:

Non-performing residential mortgages by average loan to value (LTV)	2012 €m	2011 €m
<70%	**558**	438
>70% and <=90%	**351**	256
>90% and <=110%	**387**	294
>110% and <=130%	**468**	373
>130%	**2,117**	1,306
Total portfolio average by LTV	**132.5%**	125.1%

Performing residential mortgages by average loan to value (LTV)	2012 €m	2011 €m
<70%	**3,932**	4,534
>70% and <=90%	**2,076**	2,318
>90% and <=110%	**2,247**	2,667
>110% and <=130%	**2,552**	3,000
>130%	**6,009**	6,039
Total portfolio average by LTV	**109.5%**	105.8%

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

	2012 €m	2011 €m
Derivative assets gross exposure	32	23

23. Risk management (continued)

Regulatory risk

Regulatory risk is the risk of material loss or liability, legal or reputational sanctions, or reputational damage, arising from the failure to comply with (or adequately plan for changes to) relevant official sector policy, laws, regulations, or major industry standards, in any location in which the Group operates. The Group believes that maintaining a strong regulatory risk framework is fundamental to protecting sustainable growth, rebuilding its reputation and maintaining stakeholder confidence.

The regulatory environment remained highly challenging during 2012, as policymakers and regulators continued to strengthen regulation and supervision in response to the events of 2007 and 2008 and subsequent economic and financial stress.

The Group's approach to regulatory risk has three distinct elements:

- The review of potential changes in regulation to ensure that the Group addresses the risks arising from such changes and responds appropriately;
- The monitoring of compliance with existing rules and regulations and the mitigation of the consequences of any inadvertent non-compliance; and
- The management of effective relationships with regulators to ensure constructive engagement.

Reputational risk

Reputational risk is the risk of brand damage and/or financial loss due to a failure to meet stakeholders' expectations of the Group's conduct and performance.

Stakeholders include customers, investors, rating agencies, employees, suppliers, government, politicians, regulators, special interest groups, consumer groups, media and the general public. Brand damage can be detrimental to the business in a number of ways, including an inability to build or sustain business relationships, low staff morale or reduced access to funding sources.

One of the most fundamental stakeholder expectations is that a bank is financially prudent, safe and sound. The Group has made significant progress in restructuring its balance sheet and improving its capital and funding position. Major reforms have also been made to strengthen its risk evaluation and management processes. Further work remains, but the Group is now in a much stronger financial position to face challenges and uncertainties in its economic and operating environment.

The Group has put the focus on serving customers well at the heart of its strategic objectives that, combined with a safe and sound bank, will build a culture and reputation in line with our stakeholder expectations. There are still legacy issues to work through, but dealing with them in an open and direct manner is a necessary part of the ability to move forward.

The Group's reputational risk management framework is aligned with its strategic objectives and its risk appetite. It is designed to embed, at different points of decision-making processes, a series of customer-related and reputational filters and controls that examine products, services and activities through the lens of sustainability, transparency and fairness.

This approach recognises that reputational risk can arise across a range of actions taken (or, in some cases, not taken) by the Group, as well as its wider conduct, policies and practices. Therefore, it is aligned with the management of a range of risk types that have a high reputational sensitivity.

The Board has ultimate responsibility for managing the Group's reputation, though all parts of the Group have responsibility for any reputational impact arising from their operations.

23. Risk management (continued)

Conduct risk

Conduct risk is the risk that the conduct of the Group and its staff towards its customers, or within the markets in which it operates, leads to reputational damage and/or financial loss by breaching regulatory rules or laws, or failing to meet customers' or regulators' expectations of the Group. Activities through which conduct risk may arise include: personal account dealing; privacy and data protection; conflicts of interest; and product design.

Effective conduct risk management is not only a commercial imperative for the Group; customers, clients and counterparties demand it as a precursor to building trust. It also reflects the changing regulatory environment.

The RBS Group's Compliance function manages conduct risk facing the Group, including Anti-Money Laundering (AML); Sanctions and Terrorist Financing; and Anti-Bribery and Corruption. In doing so, Group Compliance is responsible for the design, implementation and maintenance of an effective management framework to enable consistent identification, assessment, management, monitoring and reporting of conduct risk.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. It is an integral and unavoidable part of the Group's business as it is inherent in the processes it operates to provide services to customers and meet strategic objectives.

The objective of operational risk management is not to remove operational risk altogether, but to manage it to an acceptable level, taking into account the cost of minimising the risk against the resultant reduction in exposure. Strategies to manage operational risk include avoidance, transfer, acceptance and mitigation by controls.

In 2012, the Group continued to make good progress in enhancing its operational risk framework and risk management capabilities.

The standards, which are incorporated in the Group Policy Framework, provide the direction for delivering effective operational risk management and are designed to allow the consistent identification, assessment, management, monitoring and reporting of operational risk across the Group.

Operational risk appetite, policy and frameworks are tabled regularly at the Executive Risk Forum to satisfy oversight responsibilities and, as appropriate, to other senior committees.

Sovereign risk

The Group's sovereign portfolio comprises central governments, central banks and sub-sovereigns such as local authorities, primarily in the Group's key market in the Republic of Ireland. Exposure predominantly comprises cash balances placed with central banks such as the Bank of England, the Central Bank of Ireland and consequently, the asset quality of this portfolio is high. Exposure to sovereigns fluctuates according to the Group's liquidity requirements and cash positions, which determine the level of cash placed with central banks.

Pension risk

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

The Ulster Bank Pension Scheme (Republic of Ireland) (UBPSROI) is the largest of the schemes and the main source of pension risk. It operates under trust deeds under which the corporate trustees are wholly owned subsidiaries of the Group. The trustee boards comprise six directors selected by the Group and three directors nominated by members.

The trustee board is solely responsible for the investment of the scheme's assets which are held separately from the assets of the Group. The Group and the trustee board must agree on the investment principles and the funding plan.

23. Risk management (continued)

Pension risk (continued)

In November 2009, the scheme was closed to new employees. In April 2010, the Group confirmed that it was making changes to the scheme and the Group's other defined benefit scheme, the First Active Pension Scheme (FAPS). For some members, the Group has limited the amount by which pensionable salary would increase in future (the "pensionable salary cap") to 2% per annum (or CPI inflation, if lower). For those who decided not to accept terms which included the pensionable salary cap, and were not in the Provident Fund sections of the schemes, the Group agreed with the trustees of the schemes a reduction in the accrual rate from 60ths to 80ths for future service, in return for improvements in future funding of the schemes. In 2011 a further contract offer was made and this has reduced the number of employees who are subject to the lower accrual rate and increased the number subject to the pensionable earnings cap.

Risk appetite and investment policy are agreed by the trustees with quantitative and qualitative input from the scheme actuaries and investment advisers. The trustees also consult with the Group to obtain its view on the appropriate level of risk within the pension funds. The Group independently monitors risk within its pension funds as part of the Internal Capital Adequacy Assessment Process.

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

The most recent funding valuations of the UBPSROI scheme was carried out 31 December 2009. Further details are given in Note 4 to the accounts. As a result of a change in the funding framework in the Republic of Ireland, new funding plans for the UBPSROI and FAPS need to be submitted by 30 June 2013. These revised funding plans may result in a change in the level of contributions payable to the schemes.

With effect from 1 January 2013, the revised International Accounting Standard for Pensions (IAS19R) will apply to the schemes. As a result the current "corridor" methodology adopted by the Group which permitted deferral of recognition of gains and losses within a 10% corridor will be abolished. From 2013 onwards, gains and losses will be immediately recognised, resulting in increased balance sheet volatility.

24. Capital resources

The following table analyses the Group's regulatory capital resources at 31 December:

	2012 €m	2011 €m
Shareholders' equity (excluding non-controlling interests)	8,223	7,222
Non-controlling interests	-	-
Non-controlling interests per balance sheet	24	23
Other adjustments to non-controlling interests for regulatory purposes	(24)	(23)
Regulatory adjustments	(3,051)	(2,667)
Defined benefit pension adjustment	(92)	(53)
Unrealised losses on AFS debt securities	-	(1)
Other adjustments for regulatory purposes	(64)	(113)
50% excess of expected losses over impairment	(1,873)	(1,691)
Excess on Tier 2 deduction taken to Tier 1	(1,022)	(809)
Total tier 1 capital	5,172	4,555
Qualifying tier 2 capital	851	882
Undated subordinated debt	115	114
Dated subordinated debt – net of amortisation	736	761
Collectively assess impairment allowances	-	7
Tier 2 deductions	(851)	(882)
50% excess of expected losses over impairment	(1,873)	(1,691)
Excess on Tier 2 deduction taken to Tier 1	1,022	809
Total tier 2 capital	-	-
Total regulatory capital	5,172	4,555
Key capital ratios	%	%
Tier 1	11.4	10.3
Total capital	11.4	10.3
Risk weighted assets by risk		
Credit risk	41,252	40,809
Counterparty risk	2,122	1,657
Market risk	181	309
Operational risk	1,735	1,616
Risk weighted assets	45,290	44,391

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

In carrying out these policies the Group has regard to and has complied with the supervisory requirements of the Central Bank of Ireland (CBI). The CBI uses Risk Asset Ratio (RAR) as a measure of capital adequacy for Republic of Ireland banks, 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 not be less than 8% with a Tier 1 component of not less than 4%.

Ulster Bank Ireland Ltd was fined €1.96m by the CBI in November 2012 in respect of a temporary contravention of certain capital and liquidity reporting regulations in 2011.

25. Memorandum items

Contingent liabilities and commitments

The amounts shown in the table below are intended only to provide an indication of the volume of business outstanding at 31 December 2012. 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	
	2012	2011
	€m	€m
Contingent liabilities:		
Guarantees and assets pledged as collateral security	**285**	426
Other contingent liabilities	**241**	225
	526	651
Commitments:		
Documentary credits and other short-term trade related transactions	**8**	6
Commitments to lend		
less than one year	**1,620**	1,804
one year and over	**1,141**	1,037
	2,769	2,847

Banking commitments and contingent obligations, which have been entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities. The Group's maximum exposure to credit loss, in the event of non-performance by the other party and where all counterclaims, collateral or security proves valueless, is represented by the contractual nominal amount of these instruments included in the table. These commitments and contingent obligations are subject to the Group's normal credit approval processes and any potential loss is taken into account in assessing provisions for bad and doubtful debts in accordance with the Group's provisioning policy.

Contingent liabilities

Guarantees - the Group gives guarantees on behalf of customers. A financial guarantee represents an irrevocable undertaking that the Group will meet a customer's obligations to third parties if the customer fails to do so. The maximum amount that the Group could be required to pay under a guarantee is its principal amount as disclosed in the table above. The Group expects most guarantees it provides to expire unused.

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.

Commitments

Commitments to lend - 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, documentary credits and other short-term trade related transactions.

25. Memorandum items (continued)

Commitments (continued)
Regulatory enquiries and investigations - in the normal course of business the Group and its subsidiaries co-operate with regulatory authorities in various jurisdictions in their enquiries or investigations into alleged or possible breaches of regulations.

Additional contingent liabilities arise in the normal course of the Group's business. It is not anticipated that any material loss will arise from these transactions.

The Bank has given guarantees under Section 17 of the Companies (Amendment) Act, 1986 of the Republic of Ireland in respect of:

Cherbou Property Limited *(in voluntary liquidation)*
Cuvia Finance Limited
Danroc Limited
Easycash (Ireland) Limited
First Active Insurance Services Limited
First Active Investments No.4 Limited
GMM Property Limited
Hume Street Nominees Limited
Meritvale Limited
Norgay Property Limited
Sanlar *(in voluntary liquidation)*
The RBS Group Ireland Retirement Savings Trustee Limited
UB SIG (ROI) Limited
UIF Finance Company
Ulster Bank Group Treasury Limited
Ulster Bank Investment Funds Limited
Ulster Bank Wealth
Ulster Bank Wealth Nominees Limited
Ulster International Finance
Walter Property Limited
West Register (ROI) Property Realisations Limited
West Register (Republic of Ireland) Property Limited

Contractual obligations for future expenditure not provided in the financial statements

The following table shows contractual obligations for future expenditure not provided for in the financial statements at the year end:

	Group		Bank	
	2012	2011	**2012**	2011
	€m	€m	**€m**	€m
Contracts to purchase goods or services	**5**	6	**5**	5

Litigation

The Group is involved in litigation in the Republic of Ireland. The litigation involves claims by and against Group companies which arise in the ordinary course of business. No material adverse effect on the net assets of the Group is expected to arise from the ultimate resolution of these claims.

Interest rate hedging products
Ulster Bank Ireland Limited has recently been served with two litigation claims in relation to interest rate hedging products in the Republic of Ireland.

26. Net cash flow from operating activities

	Group		Bank	
	2012	2011	**2012**	2011
	€m	€m	**€m**	€m
Operating loss before tax	**(2,141)**	(2,811)	**(2,096)**	(2,945)
Depreciation, amortisation and impairment	**33**	23	**30**	20
Interest on subordinated liabilities	**32**	35	**19**	19
Charge for defined benefit pension scheme	**23**	23	**23**	23
Cash contribution to defined benefit pension schemes	**(45)**	(42)	**(45)**	(42)
Loan impairment provisions net of recoveries	**2,311**	3,235	**2,311**	3,235
Elimination of foreign exchange differences	**14**	32	**8**	34
Other non-cash items	**(224)**	(267)	**(229)**	(292)
Net cash flow from trading activities	**3**	228	**21**	52
Decrease in loans and advances to banks and customers	**1,964**	1,669	**1,797**	497
Decrease in debt securities	**22**	15	**1,490**	2,703
Decrease in other assets	**(61)**	(19)	**(67)**	(43)
Decrease/(increase) in derivative assets	**262**	(88)	**145**	(81)
Changes in operating assets	**2,187**	1,577	**3,365**	3,076
Decrease in deposits by banks and customers	**(3,994)**	(5,339)	**(5,488)**	(9,553)
(Decrease)/increase in debt securities in issue	**(186)**	(1,939)	**20**	(175)
(Decrease)/increase in other liabilities	**(28)**	8	**(22)**	34
(Decrease)/increase in derivative liabilities	**(413)**	29	**(249)**	64
Changes in operating liabilities	**(4,621)**	(7,241)	**(5,739)**	(9,630)
Total taxes (paid)/received	**(54)**	40	**(52)**	15
Net cash outflow from operating activities	**(2,485)**	(5,396)	**(2,405)**	(6,487)

27. Interest received and paid

	Group		Bank	
	2012	2011	**2012**	2011
	€m	€m	**€m**	€m
Interest received	**1,264**	1,078	**1,431**	1,306
Interest paid	**(547)**	(710)	**(821)**	(1,056)
	717	368	**610**	250

28. Analysis of changes in financing during the year

	Group and Bank					
	Share capital and share premium		Capital contribution reserve		Subordinated liabilities	
	2012	2011	**2012**	2011	**2012**	2011
	€m	€m	**€m**	€m	**€m**	€m
At 1 January	**4,734**	4,734	**9,127**	4,512	**946**	934
Net cash inflows from financing	**-**	-	**3,358**	4,615	**-**	-
Currency translation and other adjustments	**-**	-	**-**	-	**10**	12
At 31 December	**4,734**	4,734	**12,485**	9,127	**956**	946

29. Analysis of cash and cash equivalents

	Group		Bank	
	2012	2011	**2012**	2011
	€m	€m	**€m**	€m
At 1 January				
Cash	**272**	279	**272**	279
Cash equivalents	**2,998**	3,633	**1,845**	3,559
	3,270	3,912	**2,117**	3,838
Net cash inflow/(outflow)	**832**	(644)	**929**	(1,723)
Effect of exchange rate changes on cash and cash equivalents	**23**	2	**21**	2
At 31 December	**4,125**	3,270	**3,067**	2,117
Comprising:				
Cash and balances at central banks	**221**	272	**221**	272
Loans and advances to banks and debt securities	**3,904**	2,998	**2,846**	1,845

30. Divisional analysis

The Group operates in the financial services industry in the Republic of Ireland and provides an integrated service to its customers. The directors manage the Group primarily by class of business and present the divisional analysis on that basis. Divisions charge market prices for services rendered to other parts of the Group; funding charges between divisions are determined by Group Treasury, having regard to commercial demands.

The Group reports on a divisional basis as follows:

Retail Banking provides loan and deposit products through a network of branches and direct channels.

Corporate Banking provides services to business and corporate customers.

Both Retail and Corporate Banking are supported by business services, finance, human resources and other head office functions.

Other comprises Non-Core and Central functions. Non-Core consists of assets that the Group intends to run off or dispose. Central functions comprise Group and corporate functions such as treasury, funding and finance, risk management, legal, communications and human resources.

ULSTER BANK IRELAND LIMITED

NOTES TO THE FINANCIAL STATEMENTS *for the year ended 31 December 2012*

30. Divisional analysis (continued)

Divisional information by class of business and geographical area is set out below:

Class of Business

	Total income			Operating expenses before depreciation	Depreciation and amortisation	Impairment losses	Operating loss before tax
	Interest income	Non-interest income	Total				
2012	**€m**	**€m**	**€m**	**€m**	**€m**	**€m**	**€m**
Retail Banking	256	46	302	(102)	-	(818)	(618)
Corporate Banking	226	107	333	(106)	-	(717)	(490)
Other	152	99	251	(360)	(22)	(902)	(1,033)
Total	**634**	**252**	**886**	**(568)**	**(22)**	**(2,437)**	**(2,141)**

Class of Business

	Total income			Operating expenses before depreciation	Depreciation and amortisation	Impairment losses	Operating loss before tax
	Interest income	Non-interest income	Total				
2011	€m	€m	€m	€m	€m	€m	€m
Retail Banking	302	61	363	(92)	(1)	(684)	(414)
Corporate Bank	333	88	421	(98)	(2)	(746)	(425)
Other	78	273	351	(320)	(20)	(1,983)	(1,972)
Total	713	422	1,135	(510)	(23)	(3,413)	(2,811)

Class of Business	**2012**		2011	
	Assets	**Liabilities**	Assets	Liabilities
	€m	**€m**	€m	€m
Retail Banking	**19,544**	**(8,707)**	20,548	(7,916)
Corporate Banking	**10,025**	**(12,566)**	11,931	(11,374)
Other	**11,343**	**(11,391)**	12,157	(18,101)
Total	**40,912**	**(32,664)**	44,636	(37,391)

Geographical divisions	**United Kingdom**	**Republic of Ireland**	**Total**	United Kingdom	Republic of Ireland	Total
	2012	**2012**	**2012**	2011	2011	2011
	€m	**€m**	**€m**	€m	€m	€m
Total Income	**54**	**832**	**886**	69	1,066	1,135
Operating loss before tax	**(110)**	**(2,031)**	**(2,141)**	(392)	(2,419)	(2,811)
Net Assets	**104**	**8,144**	**8,248**	207	7,038	7,245
Total Assets	**2,417**	**38,495**	**40,912**	2,336	42,300	44,636

31. Transactions required to be disclosed under Sections 41 and 43 of the Companies Act 1990

Transactions, agreements entered into by authorised institutions in respect of loans to persons who were directors of the Bank (or persons connected with them) at any time during the financial period were as follows:

Directors

Name of director	Principal and interest: As at 1 January (or date of appointment if later) €	Principal and interest: As at 31 December €	Maximum liability during the year €	Interest due but not yet paid €	Provision €
J Brown (1)	15,716	13,449	21,348	-	-
S Dorgan (1)	9,498	8,092	9,835	-	-
E Gleeson (1)	374	302	2,361	-	-
D O'Shea (1)	645,026	639,049	675,237	-	-

Notes:
(1) Personal & mortgage loans

Connected parties

The amounts required to be disclosed during the period pursuant to the provisions of the Companies Act 1990 (as amended by the Companies (Amendment) Act 2009) or the CBI are as follows:

As at 31 December	Maximum liability during the year
€212,299	€225,328

There were no guarantees, security or arrangements involving a guarantee or security entered into by authorised institutions in the Group in respect of guarantees to persons who were directors of the Bank (or persons connected with them) at any time during the financial period.

At 31 December 2012, the total amount outstanding under any arrangement by the Bank with any director or person connected to a director was less than 10% of the Bank's total assets.

There were no amounts outstanding at 31 December 2012 (2011: €nil) in respect of loans made to directors by subsidiary undertakings which were not authorised institutions.

32. Directors' and secretaries' interest in shares

	RBS Group							
	As at 1 January 2012 (or date of appointment if later)				As at 31 December 2012			
	Ordinary Shares of Stg 25p each				Ordinary Shares of Stg 100p each*			
	Ordinary Shares	Options **	Long Term Incentive Awards***	Deferred Stock Awards	Ordinary Shares	Options**	Long Term Incentive Awards***	Deferred Stock Awards
R Curran (Secretary)	14,068	35,077	216,677	13,111	2,033	3,507	13,405	-
E Dignam (Deputy Secretary)	-	8,919	-	8,939	427	891	-	-
S Bell	2,743	-	-	26,790	274	-	-	2,679
J Brown	217,725	37,039	1,510,446	426,745	70,114	5,016	288,187	42,820
D O'Shea	3,665	-	-	-	3,665	-	-	-

No other current director had an interest in the shares of The Royal Bank of Scotland Group plc at 31 December 2012, at 1 January 2012 or date of appointment if later.

* At The Royal Bank of Scotland Group plc Annual General Meeting on 30 May 2012 shareholders approved the share sub-division and consolidation of the RBS Group's ordinary shares, which subsequently took effect on 6 June 2012. As a result, shareholders now hold one new ordinary share for every ten existing ordinary shares held as at 1 June 2012. The nominal value of the ordinary shares was amended to £1.

** Options granted may include awards under the Irish Sharesave Plan which are not subject to performance conditions and awards under the Executive Share Option Plan which are exercisable subject to the achievement of performance conditions.

*** Vesting for these awards is subject to the achievement of performance conditions. Long Term Incentive Awards include awards granted under both the Long Term Incentive Plan and the Restricted Share Plan. No further awards will be granted under the Restricted Share Plan as it has been replaced by the Long Term Incentive Plan.

32. Directors' and secretaries' interest in shares (continued)

	Debentures	
	As at 1 January 2012 (or date of appointment if later £	As at 31 December 2012 £
Deferred Stock Awards		
R Curran (Secretary)	11,383	-
E Dignam (Deputy Secretary)	1,313	-
S Bell	91,247	8,040
J Brown	175,197	158,340

33. Related parties

The Bank's immediate parent company is Ulster Bank Holdings (ROI) Limited.

The Bank's ultimate holding company, and the parent of the largest group into which the Bank is consolidated, is The Royal Bank of Scotland Group plc which is incorporated in Great Britain and registered in Scotland. Copies of the consolidated financial statements for The Royal Bank of Scotland Group plc can be obtained from The Secretary, The Royal Bank of Scotland Group plc, Gogarburn, Edinburgh, EH12 1HQ.

The smallest subgroup into which the Bank is consolidated is Ulster Bank Limited, a company incorporated in Northern Ireland. Copies of the consolidated financial statements for this subgroup can be obtained from the Secretary, Ulster Bank Limited, 11-16 Donegall Square East, Belfast, BT1 5UB.

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 the year the Group had the following transactions with related parties:

(a) Directors and key managers

At 31 December 2012, amounts advanced by the Bank were €660,892 in respect of loans to 4 persons who served as directors during the financial period.

The aggregate transactions between the Bank and its directors, key managers, their close families and companies which they control were:

	Number of directors	Number of key managers	Connected parties	Transaction €
Transactions during the year				
Loans made during the year:				
– at a commercial rate	-	1	-	436,500
Balances outstanding at the end of the year				
Loans:				
– at a commercial rate	4	7	4	2,829,785
– at a preferential rate	-	4	-	425,725
Customer accounts:				
– Savings	5	14	18	6,035,766

33. Related parties (continued)

(b) Related party transactions

Included in the Group and Bank's balance sheet are the following balances with related parties at the year end:

	Group		Bank	
	2012 €m	2011 €m	**2012 €m**	2011 €m
Assets				
Loans and advances:				
Parent companies	**3,799**	1,443	**2,732**	314
Key management	**2**	2	**2**	2
Other related parties, including fellow subsidiaries	**527**	359	**14,103**	15,152
	4,328	1,804	**16,837**	15,468
Derivatives:				
Parent companies	**531**	818	**528**	698
Total assets	**4,859**	2,622	**17,365**	16,166
Liabilities				
Deposits:				
Parent companies	**3,431**	10,275	**3,364**	10,288
Key management	**4**	3	**4**	3
Other related parties, including fellow subsidiaries	**1,331**	576	**18,345**	19,000
	4,766	10,854	**21,713**	29,291
Subordinated Loans:				
Parent companies	**616**	615	**616**	615
Other related parties, including fellow subsidiaries	**340**	331	**340**	331
	956	946	**956**	946
Derivatives:				
Parent companies	**1,178**	1,540	**995**	1,192
Total liabilities	**6,900**	13,340	**23,664**	31,429

(c) Compensation of key management

The aggregate remuneration of directors and other members of key management during the year was as follows:

	2012 €	2011 €
Short-term benefits	**2,786,051**	2,698,497
Termination benefit	**-**	336,732
Long-term benefit	**589,643**	627,648
	3,375,694	3,662,877

34. Post balance sheet events

There have been no significant events between the year end and the date of approval of the financial statements which would require a change or additional disclosure or amendment in the financial statements.

35. Date of approval

The financial statements were approved by the Board of Directors on 22 February 2013.